IN THE

Supreme Court of the United States

OCTOBER TERM, 1973

No. 73-5265

HENRY A. KOKOSZKA,

Petitioner,

—v.—

RICHARD BELFORD, Trustee in Bankruptcy of the Estate of Henry A. Kokoszka, Bankrupt,

Respondent.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

INDEX

Relevant Docket Entries

Date	Docket Entry
1- 5-72	Petition and Schedules, filed at 3:12 p.m.
2- 3-72	Referee's order re income tax refund
2- 7-72	Motion for Rehearing
3-24-72	Referee's order on Motion for Rehearing
4- 3-72	Petition for Review filed
4-11-72	Certificates of Referee on Petition for Review filed
7-24-72	Memorandum of Decision filed and entered. The Petition for Review is denied and the order of the Referee is confirmed. (Newman, J.)
8-21-72	Petition for Allowance of Appeal filed
8-21-72	Motion for leave to proceed in forma pauperis
9- 5-72	Petition for allowance of appeal granted
9- 5-72	Motion for leave to proceed in forma pauperis granted
5-18-73	Appeal affirmed in part; reversed in part

UNITED STATES DISTRICT COURT
DISTRICT OF CONNECTICUT

In Bankruptcy

No. 37437

In the Matter of

HENRY ANTHONY KOKOSZKA, BANKRUPT

ORDER RE INCOME TAX REFUND AND DEFERMENT OF BANKRUPT'S DISCHARGE

It appearing that the bankrupt may be entitled to an income tax refund from Internal Revenue Service on taxes withheld from wages or otherwise paid prior to bankruptcy, it is

ORDERED that:

(a) the bankrupt shall promptly file with the trustee in bankruptcy a copy of his income tax return for the year 1971 if it has now been prepared, or shall do so as soon as the return is prepared;

(b) the bankrupt shall do all things requisite to assist the trustee in bankruptcy in recovering any such refund;

(c) the bankrupt shall forthwith deliver to the trustee in bankruptcy any tax refund that may be paid to the bankrupt;

(d) the trustee in bankruptcy shall promptly notify Internal Revenue Service of his right to any tax refund now or eventually due to the bankrupt; and,

(e) entry of the bankrupt's discharge in bankruptcy, if eventually he be entitled thereto, shall be deferred until the bankrupt has complied with this order.

Dated at Bridgeport, February 3, 1972

R. E. TREVETHAN
Referee in Bankruptcy

UNITED STATES DISTRICT COURT
DISTRICT OF CONNECTICUT

[Title Omitted]

MOTION FOR REHEARING

The petitioner herein moves that this court grant a rehearing with regard to its order of February 3, 1972, directing that the bankrupt turn over his tax refund to the trustee in bankruptcy. The petitioner wishes to present evidence as to the amount of income withheld, the reasons therefor, and the employment record of petitioner.

Upon hearing said evidence, petitioner requests that the order of February 3, 1972 be vacated for the following reasons:

1. Said tax refund is not "property" within the meaning of sections 70a(5) and 70a(6) of the Bankruptcy Act. *Frederick* v. *Lines*, 400 U.S. 18 (1970).
2. Said tax refund is not so rooted in the pre-bankruptcy past as to constitute property within the meaning of sections 70a(5) and 70a(6) of the Bankruptcy Act, or *Segal* v. *Rochelle* et seq. 382 U.S. 375 (1966).
3. Said order is inconsistent with the purposes of the Bankruptcy Act in that it hinders the bankrupt from an unencumbered fresh start.
4. Said tax refund is the equivalent of future wages.

THE PETITIONER

By:

FRANCIS X. DINEEN
His Attorney

[Certificate of Service Omitted in Printing]

UNITED STATES DISTRICT COURT
DISTRICT OF CONNECTICUT

In Bankruptcy

No. 37437

In the Matter of

HENRY ANTHONY KOKOSZKA, BANKRUPT
ORDER ON MOTION FOR REHEARING

By its customary order entered *ex parte* on February 3, 1972 this court directed the bankrupt, among other things, to turn over to the trustee in bankruptcy any tax refund he might receive on his 1971 federal income taxes. On February 7, 1972 the bankrupt filed a motion requesting a rehearing on this order and that it be vacated on the grounds that (a) the tax refund is not property within sections 70a(5) and 70a(6) of the Bankruptcy Act and case law, (b) the order is inconsistent with the purposes of the Bankruptcy Act in that it hinders the bankrupt from an unencumbered fresh start, and (c) the tax refund is the equivalent of future wages.

Duly noticed hearing was held on the motion at which the bankrupt and the trustee in bankruptcy appeared. The evidence offered at the hearing is as follows. The bankrupt was employed for approximately the first three months of 1971, was unemployed from April, 1971 to late December, 1971 and received unemployment compensation, and then was reemployed and worked about the last week and a half of December, 1971. During the year 1971 the bankrupt had two exemptions for federal income tax purposes, and the bankrupt told his employer that he was taking his two exemptions on the tax withholdings from his pay.

The bankrupt's federal income tax return for 1971 sets forth that he is entitled to a tax refund of $250.90. Presumably. this refund arises because the periodic withholdings from the bankrupt's pay were under a tax table geared to total annual compensation which was more than the bankrupt actually earned.

The bankrupt needs either an operation for a hernia or some form of abdominal supporter, dental work and he could use eyeglasses for distance when walking. His wife has not worked in the past twenty four years.

Until recent days it was thought "firmly established that the bankruptcy trustee succeeds to any claim or right of action the bankrupt may have against the Government for a refund of taxes paid" (4A *Collier*, Bankruptcy, par. 70.28(4) and authorities cited in note 27). Consistent with this concept, a trustee in bankruptcy acquires title to a claim a bankrupt may have for a tax refund based on the loss-carryback provisions of the Internal Revenue Code when applied to taxes paid by a bankrupt prior to bankruptcy (*Segal* v. *Rochelle*, 1966, 382 U.S. 375). But, in view of the recent case of *Lines* v. *Frederick*, 1970, 400 U.S. 18, the bankrupt here claims that a tax refund arising out of an excess of tax withholding by an employer from the wages of a bankrupt-employee remains the property of the employee and does not pass to the trustee in bankruptcy.

The *Lines* case involved the question of whether a bankrupt wage earner's vacation pay, accrued but unpaid at the time of bankruptcy, passes to the trustee in bankruptcy as property under section 70a(5) of the Bankruptcy Act or remains the property of the bankrupt. The court reviewed the *Segal* case, *supra*, and commented that the tax refund claim in that case arose out of business operations and was "sufficiently rooted in the pre-bankruptcy past and so little entangled with the bankrupt's ability to make an unencumbered fresh start that it should be regarded as 'property' under sec. 70a(5)". The court then proceeded as follows:

> By contrast, the respondents here are wage earners whose sole source of income, before and after bankruptcy, is their weekly earnings. The function of their accrued vacation pay is to support the basic requirements of life for them and their families during brief vacation periods or in the event of layoff. Since it is a part of their wages, the vacation pay is "a specialized type of property presenting distinct problems in our economic system" (case cited).

> Where the minimal requirements for the economic survival of the debtor are at stake, legislatures have recognized that protection that might be unnecessary or unwise for other kinds of property may be required . . . .
>
> The wage-earner bankrupt who must take a vacation without pay or forego a vacation altogether cannot be said to have achieved the "new opportunity in life and (the) clear field for future effort, unhampered by the pressure and discouragement of preexisting debt," (case cited) which it was the purpose of the statute to provide.

To resolve the issue here presented requires an analysis of the *Lines* case in the light of the basic statutory law and the *Segal* case.

A trustee in bankruptcy is vested by operation of law with the title of the bankrupt as of the date of bankruptcy to property, including rights of action, which prior to bankruptcy the bankrupt could have transferred by any means (Bankruptcy Act, sec. 70a(5)55. In *Segal* the court observed that:

> The main thrust of section 70a(5) is to secure for creditors everything of value the bankrupt may possess in alienable or leviable form when he files his petition. To this end the term "property" has been construed most generously and an interest is not outside its reach because it is novel or contingent or because enjoyment must be postponed.

The court also remarked that, on the other hand, one highly prominent purpose of the Bankruptcy Act "is to leave the bankrupt free after the date of his petition to accumulate *new* wealth in the *future* (underlining added)." It then concluded that the loss-carryback refund claim was "sufficiently rooted in the pre-bankruptcy past and so little entangled with the bankrupts' ability to make an unencumbered fresh start that it should be regarded as 'property' under section 70a(5)."

Returning to the *Lines* case we must now endeavor to extract from the essentials of what was there said—already set forth earlier in this opinion—the basic and

controlling concept which it pronounces. As this court analyses it, *Lines* laid down the precept that an exception from the impact of section 70a(5) must be judicially carved out for accrued vacation pay because of its *prospective purpose* as *future support* for the wage-earner's basic requirements for living and caring for his family during vacations or a layoff. To take away his accrued vacation pay, specifically designed and intended for the future acquisition of the necessities of life during a period when the wage-earner was not at his labor, would be tantamount to an appropriation by a trustee in bankruptcy of what in fact had all the flavor of future wages acquired after bankruptcy. Thus, as this court views it, *Lines* rests upon the thought that wages earned and held specifically for the future support of the bankrupt and his family during a foreseeable period away from daily labor should be held for that purpose insulated from alienation by creditors.

It is this court's belief that there are such marked differences between the nature of a claim to a tax refund and that of accrued vacation pay as evolved by *Lines* that the concept of *Lines* cannot logically or sensibly be extended to embrace a claim to a tax refund as a further judically conceived exception to section 70a(5) of the Act. First, wages are withheld under federal law for application on an eventual tax liability and are paid to and become the property of the government. Second, the wages are not withheld for taxes under any designed program that they or any portion of them shall be returned to the bankrupt to insure his future support when he is without daily earnings. Third, a claim to a refund arising out of taxes voluntarily or involuntarily paid out of wages is quite the equivalent of savings accumulated by a bankrupt out of his yearly earnings and any such savings held by a bankrupt at bankruptcy—whether in the form of cash in a safe deposit box or in a bank account—became the property of the bankruptcy estate. Fourth, a claim to a refund is not distinguishably different from any other property or property right which a bankrupt might have acquired by using a portion of his annual wages to make a loan to another, to buy se-

curities or to acquire an automobile, all of which pass to a trustee in the event of bankruptcy. Accordingly, it is the view of this court that a claim to a tax refund for excess taxes paid from wages is quite something different from a right to receive accumulated wages in the future which were specifically designed to substitute for future lack of earnings. The concept of *Lines* is not applicable to a tax refund. Such a refund is a property which passes to a trustee in bankruptcy under section 70a(5).

This court also finds unacceptable the contention that a distinction is to be drawn between a claim for tax refund based on wages withheld in the amounts fixed by the federal tax withholding tables and a claim wholly or partially resulting from withholdings in excess of the amounts required by the tax tables. One court has seen fit to draw this distinction (*Matters of Cedor and James*, #2-70 287 ACW and #3-70 1064 ACW, D.C.N.D. Calif., 1/20/72). However, flowing from all which this court has already said in this opinion, it is its conclusion that a claim to a tax refund, however it may have been created, is quite something different from, and does not fall within the ambit of, the concept of accrued vacation pay as developed in the *Lines* case.

Finally, it is the view of this court that the wage garnishment provisions of the Consumer Credit Protection Act (Consumer Act) (15 USC sec. 1671 *et seq*) do not have any impact to limit a bankruptcy estate to 25% of a tax refund and to give the bankrupt 75% thereof. This court is compelled to disagree with the contrary position taken in the *Matters of Cedor and James, supra.*

Reading the Consumer Act as a cohesive entity, it is concluded that its sole purpose and effect is restricted to wage garnishment procedures as they have been historically understood to limit to 25% the amount that periodically may be taken from a person's current and future weekly take-home pay to be applied against an indebtedness. The opening section of the Consumer Act (15 USC sec. 1671) sets forth the findings of Congress that "unrestricted garnishment of compensation due for

personal services" encourages extension of credit, and that the "application of garnishment as a creditor's remedy frequently results in loss of employment by the debtor". Encouragement of credit and loss of employment may result from the normal wage garnishment which regularly takes a portion of a debtor's pay as it falls due. This court cannot conceive that either can result from the passage of a debtor's tax refund to his bankruptcy estate.

The next section of the Consumer Act (15 USC sec. 1672) defines "garnishment" to mean "any legal or equitable procedure through which the earnings of any individual are required to be withheld for payment of any debt", and the term "earnings" means "compensation paid or payable for personal services". These definitions demonstrate that under the Consumer Act wage garnishment procedure means what it has historically meant; it means a repetitious withholding of money from the debtor's periodic earnings for application on a debt. The claim of a trustee in bankruptcy to a bankrupt's tax refund is not a withholding of the bankrupt's earnings; the withholding occurred when the monies were taken from the bankrupt's pay to apply on his taxes. Certainly, the tax refund arises out of a use previously made of a portion of the bankrupt'a past pay, but so do property rights in stocks, bonds, automobiles or anything else acquired with previous earnings. And, surely, it would not be rational to say that a trustee's succession to these properties of a bankrupt constitute a garnishment of his earnings within the framework of the Consumer Act.

It is also provided in the Consumer Act that "disposable earnings" means that "part of the earnings of any individual remaining after the deduction from those earnings of any amounts required by law to be withheld" (15 USC sec. 1672) and that "the maximum part of the aggregate disposable earnings of an individual *for any workweek* which is subjected to garnishment may not exceed 25 per centum of his disposable earnings *for that veek* (underlining added)" (15 USC sec. 1673). It might be enough to say that here what created the claim to a tax refund was not the "disposable earnings"

of the bankrupt but the deductions from his earnings of amounts required by law to be withheld under the federal withholding tax tables. Thus, the 25% limitation on disposable earnings has no application to the earnings which created the refund. Moving to a broader view of these portions of the statute, it is apparent from the express provisions that their purpose and effect is to limit to 25% of the disposable earnings *for any workweek* the amount that may be taken by garnishment *for that week*. Such clear language compels its conclusion that the 25% limitation of the statute has application only to the amount that can be taken weekly from a debtor's pay under normal garnishment. This court finds it impossible to distort such specific language to extend it to include 25% of any claim a bankrupt may have against the government for a tax refund.

The next section of the Consumer Act (15 USC 1674) provides that "no employer may discharge any employee by reason of the fact that his earnings have been subjected to garnishment for any one indebtedness." Human experience tells us that this relates to the past practice of many employers who would discharge garnished employees because of their improvident ways and to avoid the necessary bookkeeping involved in honoring even a single weekly garnishment. Certainly, that a trustee may have a right to a bankrupt's tax refund is unrelated to personal improvidence and cannot result in the imposition of any conceivable burden upon an employer which would precipitate discharge of the employee.

And, finally, it is this court's view that—contrary to the thinking expressed in the *Matters of Cedor and James, supra,*—the provision of the Consumer Act that the 25% limitation does not apply to "any order of any court of bankruptcy under Chapter XIII of the Bankruptcy Act" cannot be interpreted to mean that the 25% limitation does embrace a tax refund. This provision relates to section 658 of Chapter XIII which gives the bankruptcy court the power to order the employer of a Chapter XIII debtor to withhold from the bankrupt's pay and turn over to the trustee whatever periodic amounts the debtor has agreed to pay to the trustee

under the terms of his wage-earner plan. It expressly leaves this judicial power unaffected by the 25% limitation on periodic withholdings from the debtor's earnings, and it has no other effect.

All in all, if a wage-earner's right to a tax refund is to be excepted from the provisions of section 70a(5) of the Bankruptcy Act, it is for Congress and not judicial authority to accomplish it.

In view of all that has been said, it is

ORDERED that the bankrupt's motion to vacate this court's order of February 3, 1972 is denied.

Dated at Bridgeport, March 24, 1972.

R. E. TREVETHAN
Referee in Bankruptcy

UNITED STATES DISTRICT COURT
DISTRICT OF CONNECTICUT

[Title Omitted]

PETITION FOR REVIEW

TO THE HONORABLE R. E. TREVETHAN, REFEREE IN BANKRUPTCY

The petition of Henry Anthony Kokoszka, Bankrupt herein, respectfully shows:

I

That your petitioner is the Bankrupt in the above-entitled proceedings.

II

That on the third day of February, 1972, this Court made and entered an Order directing that the bankrupt deliver to the trustee in bankruptcy any tax refund now due to the bankrupt; and further ordering that entry of the bankrupt's discharge in bankruptcy be deferred until compliance with said order. A copy of the complete text of said order is annexed hereto as Exhibit A and made a part hereof as though fully recited herein.

III

That on the 24th day of March, 1972, this Court, after rehearing, denied bankrupt's motion to vacate the Court's order of February 3, 1972.

IV

That your petitioner is aggrieved by said Orders and said Orders are in error in the following respects:

1. Said tax refund is not property within the meaning of §§ 70a(5) and 70a(6) of the Bankruptcy Act. *Frederick v. Lines*, 400 U.S. 18 (1970).

2. Said tax refund is not so rooted in the pre-bankruptcy past as to constitute property within the meaning of §§ 70a(5) and 70a(6) of the Bankruptcy Act, or *Segal* v. *Rochelle*, 382 U.S. 375 (1966).

3. Said order is inconsistent with the purposes of the Bankruptcy Act in that it hinders the bankrupt from an unencumbered fresh start.

4. Said tax refund is the equivalent of wages.

5. Under the Federal Consumer Credit Protection Act, the trustee is not entitled to more than 25% of the bankrupt's tax refund.

WHEREFORE, your Petitioner prays that a certificate be promptly prepared as required by law and forwarded to the Clerk of the United States District Court and that upon the hearing thereof, said Order be reversed and petitioner's bankruptcy be allowed to proceed without payment over to the trustee of his income tax refund.

THE PETITIONER

By: FRANCIS X. DINEEN

[Certificate of Service Omitted in Printing]

UNITED STATES DISTRICT COURT
DISTRICT OF CONNECTICUT

In Bankruptcy

No. 37437

In the Matter of

HENRY ANTHONY KOKOSZKA, BANKRUPT

To The Judges Of The District Court Of The United States For The District Of Connecticut.

CERTIFICATE OF REFEREE ON
PETITION FOR REVIEW

R. E. Trevethan, the Referee in Bankruptcy in charge of this proceeding, does hereby certify all that is hereafter set forth.

On February 7, 1972 the bankrupt filed a motion requesting a rehearing on the *ex parte* order entered by this court on February 3, 1972 and that the order be vacated. That order, among other things, directed the bankrupt to turn over to the trustee in bankruptcy any tax refund he might receive on his 1971 federal income taxes. Hearing was held on the bankrupt's motion and on March 24, 1972 order entered denying the bankrupt's motion to vacate the order of February 3, 1972. On April 3, 1972 the bankrupt filed a petition for review of the order of March 24, 1972.

There is hereafter set forth a statement of the questions presented, the findings of the court, its conclusions of law, the order entered by the court and a summary of the evidence. There is submitted herewith (a) the *ex parte* order of this court dated February 3, 1972, (b) the bankrupt's motion for rehearing on this order and that it be vacated, (c) the order of this court denying the motion to vacate, (d) the bankrupt's petition for review, and (e) the single exhibit in evidence.

STATEMENT OF QUESTIONS PRESENTED

The questions presented are as follows:

1. Whether a federal income tax refund of a bankrupt wage earner which resulted from an excess of withholdings from his wages under the tax tables is a property which passes to the trustee in bankruptcy, or whether it remains the property of the bankrupt.

2. If the bankruptcy estate does have some right to such tax refund, whether it is limited to receiving only 25% of the refund under the garnishment provisions of the federal Consumer Credit Protection Act.

FINDINGS OF FACT

1. This bankruptcy proceeding was commenced by voluntary petition filed by the bankrupt on January 5, 1972.

2. On February 3, 1972 this court entered its customary *ex parte* order which, among other things, direct the bankrupt to turn over to the trustee in bankruptcy any tax refund the bankrupt might receive on his 1971 federal income taxes.

3. The bankrupt was employed for approximately the first three months of 1971, was unemployed from April, 1971 to late December, 1971 and received unemployment compensation during this period, and was then re-employed and worked about the last week and a half of December, 1971.

4. During the year 1971 the bankrupt had two exemptions for federal income tax purposes, and he told his employer that he was taking his two exemptions on the tax withholdings from his pay.

5. The bankrupt's federal income tax return for 1971 sets forth a claim to a tax refund of $250.90, and presumably this refund arises because the periodic withholdings from the bankrupt's pay were under a tax table geared to a total annual compensation which was more than the bankrupt actually earned.

6. The bankrupt's wife has not been employed during the past twenty four years.

7. The bankrupt needs either an operation for a hernia or some form of abdominal support, dental work and he could use eyeglasses for distance when walking.

CONCLUSIONS OF LAW

The conclusions of law reached by this court are fully set forth in its opinion and order of March 24, 1972 which is submitted herewith and in their essentials they may be summarized as follows:

1. The claim of a bankrupt wage earner to a federal income tax refund on taxes withheld from his earnings by his employer is not in the nature of future wages designed for the support of the bankrupt and his family, but is a property or right of action of the bankrupt which passes to the trustee in bankruptcy under the express provisions of section 70a(5) of the Bankruptcy Act.

2. It is not material whether the claim to a tax refund results from compulsory withholdings from the bankrupt's pay in the amounts fixed by the federal withholding tax tables, or whether the refund arises because the bankrupt voluntarily directed his employer to withhold more from his pay than the tax law required.

3. The garnishment provisions of the federal Consumer Credit Protection Act have no impact on the right of a bankruptcy estate to a tax refund of the bankrupt and do not limit the bankruptcy estate to 25% thereof, leaving the bankrupt with 75% of the refund.

ORDER

The order entered by this court was as follows:

"ORDERED that the bankrupt's motion to vacate this court's order of February 3, 1972 is denied."

SUMMARY OF EVIDENCE

The only testimony offered was that of the bankrupt and all of it—except for his testimony that an accountant prepared his tax return—is set forth above in the

Findings of Fact. Accordingly, there is no evidence to be summarized.

The only exhibit (Bk's Ex. A) is the bankrupt's federal income tax return for the year 1971.

Dated at Bridgeport, April 7, 1972.

R. E. TREVETHAN
Referee in Bankruptcy

13 WILLIAM STREET
WALLINGFORD, CONN. 06492

Type or print EMPLOYER'S Federal identification number, name, and address above.

Copy C—
For employee's records

FEDERAL INCOME TAX INFORMATION			SOCIAL SECURITY INFORMATION		STATUS	
Federal income tax withheld	Wages paid subject to withholding in 1971*	Other compensation paid in 1971*	F.I.C.A. employee tax withheld†	Total F.I.C.A. wages paid in 1971‡	1. Single 2. Married	
250.90	2,322.00		120.34			**

EMPLOYEE'S social security number ▶ 042-03-8432

Henry Kokeszka
39 Meadow St.
Wallingford, Ct.

Type or print EMPLOYEE'S name and address (including ZIP code) above.

Name of State	State Form No.	State income tax withheld
Name of City	**City Form No.**	**City income tax withheld**

*Excludable sick pay. **Gross wages for State if different from Federal.
† Includes tips reported by employee. Amount is before payroll deductions or sick pay exclusion.
‡ Add this item to wages in reporting wages and salaries on your income tax return.
§ The social security (FICA) rate of 5.2% includes .6% for Hospital Insurance Benefits and 4.6% for old-age, survivors, and disability insurance.
¶ Includes tips reported by employee.

Uncollected Employee Tax on Tips . . . $

FORM W-2 Department of the Treasury, Internal Revenue Service

NOTICE TO EMPLOYEE

1. Income Tax Wa— —This statement is important. Copy B must be ed with your U.S. Income Tax Return for 1971 and Copy 2 must be filed with your State or City Income Tax Return for 1971. If your social security number, name, or address is stated incorrectly, correct the information on copies B and 2 and notify your employer.

2. Social Security Wages.—If your wages were subject to social security taxes, but are not shown, your social security wages are the same as wages shown under "FEDERAL INCOME TAX INFORMATION," but not more than $7,800.

3. Credit For F.I.C.A. Tax.—If more than $405.60 of F.I.C.A. (social security and hospital insurance) employee tax was withheld during 1971 because you received wages from more than one employer, the excess should be claimed as a credit against your Federal income tax. See instructions for your Federal income tax return.

4. A copy of this form has been sent to the Internal Revenue Service.

Form **1040** — Department of the Treasury / Internal Revenue Service

U.S. Individual Income Tax Return

1971

For the year January 1–December 31, 1971, or other taxable year beginning _____, 1971, ending _____, 19__

Please print or type

First name and initial (if joint return, use first names and middle initials of both) | Last name | Your social security number

Present home address (Number and street, including apartment number, or rural route) | Spouse's social security number

City, town or post office, State and ZIP code | Occupation: Yours / Spouse's

Please attach Copy B of Form W-2 to back

Filing Status—check only one:

1 ☐ Single
2 ☒ Married filing jointly (even if only one had income)
3 ☐ Married filing separately and spouse is also filing. Give spouse's social security number in space above and enter first name here ▶ _____
4 ☐ Unmarried Head of Household
5 ☐ Surviving widow(er) with dependent child
6 ☐ Married filing separately and spouse is not filing

Exemptions

	Regular	65 or over	Blind	Enter number of boxes checked
7 Yourself	☒	☐	☐	
8 Spouse (applies only if Item 2 or 6 is checked)	☒	☐	☐	▶ 2

9 First names of your dependent children who lived with you _____ Enter number ▶ _____

10 Number of other dependents (from line 33) ▶ _____

11 Total exemptions claimed ▶ 2

Income

12	Wages, salaries, tips, etc. (Attach Forms W-2 to back. If unavailable, attach explanation)	12	2322
13a	Dividends (see pages 6 and 11 of Instr.) $_____ 13b Less exclusion $_____ Balance ▶	13c	
	(If gross dividends and other distributions are over $100, list in Part I of Schedule B.)		
14	Interest. [If $100 or less, enter total without listing in Schedule B. If over $100, enter total and list in Part II of Schedule B]	14	
15	Income other than wages, dividends, and interest (from line 40)	15	
16	Total (add lines 12, 13c, 14 and 15)	16	
17	Adjustments to income (such as "sick pay," moving expense, etc. from line 45)	17	
18	Adjusted gross income (subtract line 17 from line 16)	18	2322

● See page 3 of instructions for rules under which the IRS will figure your tax.
●● If you do not itemize deductions and line 18 is under $10,000, find tax in Tables and enter on line 19.
●● If you itemize deductions or line 18 is $10,000 or more, go to line 46 to figure tax.

Tax, Payments and Credits

19	Tax (Check if from: ☐ Tax Tables 1–13, ☐ Tax Rate Sch. X, Y, or Z, ☐ Sch. D, ☐ Sch. G or ☐ Form 4726)			19	none
20	Total credits (from line 54)			20	
21	Income tax (subtract line 20 from line 19)			21	
22	Other taxes (from line 60)			22	
23	Total (add lines 21 and 22)			23	none
24	Total Federal income tax withheld (attach Forms W-2 or W-2P to back)	24	250 90		
25	1971 Estimated tax payments (include 1970 overpayment allowed as a credit)	25			
26	Other payments (from line 64)	26			
27	Total (add lines 24, 25, and 26)			27	250 90

Bal. Due or Refund

28	If line 23 is larger than line 27, enter BALANCE DUE (Pay in full with return. Make check or money order payable to Internal Revenue Service) ▶	28	
29	If line 27 is larger than line 23, enter OVERPAYMENT ▶	29	250 90
30	Line 29 to be: (a) REFUNDED (Allow at least six weeks for your refund check) ▶ 250 90		
	(b) Credited on 1972 estimated tax ▶		

Foreign Accounts

31 Did you, at any time during the taxable year, have any interest in or signature or other authority over a bank, securities, or other financial account in a foreign country (except in a U.S. military banking facility operated by a U.S. financial institution)? If "Yes," attach Form 4683. (For definitions, see Form 4683.) ▶ ☐ Yes ☒ No

Write soc. sec. no. on Check or Money Order. Attach here

Sign here

Under penalties of perjury, I declare that I have examined this return, including accompanying schedules and statements, and to the best of my knowledge and belief it is true, correct, and complete.

▶ Henry S. Kobayashi — Your signature — Date

▶ Veronica R. Kobayashi — Spouse's signature (if filing jointly, BOTH must sign even if only one had income)

▶ J. J. [illegible] — Signature of preparer other than taxpayer, based on all information of which he has any knowledge. — Date FEB [illegible]

[illegible] Conn. — Address

Bch. ex A # 37437 3/8/72 K2

19

PART I.—Additional Exemptions (Complete only for other dependents claimed on line 10)

32 (a) NAME	(b) Relationship	(c) Months lived in your home. If born or died during year, write B or D.	(d) Did dependent have income of $675 or more?	(e) Amount YOU furnished for dependent's support. If $1000, write ALL.	(f) Amount furnished by OTHERS incl. dependent.
				$	$

33 Total number of dependents listed above. Enter here and on line 10 . . . . . ►

PART II.—Income other than Wages, Dividends, and Interest

34	Business income or (loss) (attach Schedule C)	34	
35	Net gain or (loss) from sale or exchange of capital assets (attach Schedule D)	35	
36	Net gain or (loss) from Supplemental Schedule of Gains and Losses (attach Form 4797)	36	
37	Pensions and annuities, rents and royalties, partnerships, estates or trusts, etc. (attach Schedule E)	37	
38	Farm income or (loss) (attach Schedule F)	38	
39	Miscellaneous income: (a) Fully taxable pensions and annuities not reported on Schedule E—see instructions on page 7		
	(b) 50% of capital gain distributions (not reported on Schedule D)		
	(c) State income tax refunds (caution—see instructions on page 7)		
	(d) Alimony		
	(e) Other (state nature and source)		
	(f) Total miscellaneous income (add lines 39(a), (b), (c), (d) and (e))	39	
40	Total (add lines 34, 35, 36, 37, 38, and 39). Enter here and on line 15 ►	40	

PART III.—Adjustments to Income

41	"Sick pay" if included in line 12 (attach Form 2440 or other required statement)	41	
42	Moving expense (attach Form 3903)	42	
43	Employee business expense (attach Form 2106 or other statement)	43	
44	Payments as a self-employed person to a retirement plan, etc. (attach Form 2950SE)	44	
45	Total adjustments (add lines 41, 42, 43, and 44). Enter here and on line 17 ►	45	

PART IV.—Tax Computation (Do not use this part if you use Tax Tables 1–13 to find your tax.)

46	Adjusted gross income (from line 18)	46	
47	(a) If you itemize deductions, enter total from Schedule A, line 32 and attach Schedule A (b) If you do not itemize deductions, and line 46 is: (1) $10,000 or more but less than $11,538.43, enter 13% of line 46 (2) $11,538.43 or more, enter $1,500. Note: deduction under (1) or (2) is limited to $750 if married and filing separately.	47	
48	Subtract line 47 from line 46	48	
49	Multiply total number of exemptions claimed on line 11, by $675	49	
50	Taxable income. Subtract line 49 from line 48 ►	50	

(Figure your tax on the amount on line 50 by using Tax Rate Schedule X, Y or Z, or if applicable, the alternative tax from Schedule D, income averaging from Schedule G, or maximum tax from Form 4726.) Enter tax on line 19.

PART V.—Credits

51	Retirement income credit (attach Schedule R)	51	
52	Investment credit (attach Form 3468)	52	
53	Foreign tax credit (attach Form 1116)	53	
54	Total credits (add lines 51, 52, and 53). Enter here and on line 20 ►	54	

PART VI.—Other Taxes

55	Self-employment tax (attach Schedule SE)	55	
56	Tax from recomputing prior-year investment credit (attach Form 4255)	56	
57	Minimum tax (see instructions on page 8). Check here ☐, if Form 4625 is attached	57	
58	Social security tax on unreported tip income (attach Form 4137)	58	
59	Uncollected employee social security tax on tips (from Forms W-2)	59	
60	Total (add lines 55, 56, 57, 58, and 59). Enter here and on line 22 ►	60	

PART VII.—Other Payments

61	Excess FICA tax withheld (two or more employers—see instructions on page 8)	61	
62	Credit for Federal tax on special fuels, nonhighway gasoline and lubricating oil (attach Form 4136)	62	
63	Regulated Investment Company Credit (attach Form 2439)	63	
64	Total (add lines 61, 62, and 63). Enter here and on line 26 ►	64	

☆ U.S. GOVERNMENT PRINTING OFFICE 1971—O-418-139/418-134 E1 - 52 - 07 - 33 - 972

UNITED STATES DISTRICT COURT
DISTRICT OF CONNECTICUT

Bankruptcy No. 36,028

In the Matter of

HERBERT E. SANDS

Bankruptcy No. 36,197

In the Matter of

FRANK O'BRIEN

Bankruptcy No. 37,437

In the Matter of

HENRY KOKOSZKA

MEMORANDUM OF DECISION

The common substantive issue in these three separate petitions, seeking review of decisions of a Referee in Bankruptcy, is whether an income tax refund paid to a bankrupt who claimed, for withholding purposes, all of the exemptions to which he was entitled, is property within the meaning of § 70(a)(5) of the Bankruptcy Act, 11 U.S.C. § 110(a)(5). If so, the refund vests in the Trustee and is available to the creditors. Kokoszka also contends that if the refund is such property, it is subject to the garnishment provisions of the Consumer Credit Protection Act, 15 U.S.C. §§ 1601 *et seq.*

Kokoszka's petition seeks review of the Referee's decision of March 24, 1972, refusing to vacate an order previously entered on February 3. That order requires the bankrupt to turn over to the trustee in bankruptcy any refund he may receive from the payment of his 1971 federal income taxes. Similar orders were issued in the cases of Sands and O'Brien. It is not at all clear that the orders in their cases may now be attacked since, unlike Kokoszka, they did not seek review of the Referee's

tax refund order when made, but instead received and spent their refunds and thereafter sought to challenge the order by a motion to vacate in the face of a trustee's motion to deny discharge. However, Kokoszka's petition properly brings the merits of the dispute to this Court, and the decision as to his claims disposes of the other cases as well.

The issue on the merits in all three cases is whether an income tax refund has been exempted from the definition of property in the Bankruptcy Act by the rationale of the decision of the Supreme Court in *Lines* v. *Frederick*, 400 U.S. 18 (1970). In addition to Referee Trevehtan's thoughtful opinions rejecting the petitioners' contentions in these cases, the issue has been resolved against the position of the bankrupts by a District Judge in *In re Jones*, No. 4-69 Bky. 929(o) (D. Minn. Mar. 29, 1972), *leave to appeal denied* (8th Cir. May 14, 1971), *cert. denied* —— U.S. —— (1972); and by a Referee in *In re Kingswood* (Bankruutcy No. 90279, C.D. Cal. Mar. 28, 1972), and the same result was implicit in the decision of the Eighth Circuit in *In Re Wetteroff*, —— F. 2d —— (8th Cir. Jan. 13, 1972). One District Judge has ruled in favor of the position of the bankrupts, *In re Cedor and James*, —— F. Supp. —— (N.D. Cal. Jan. 20, 1972).

The contention of the bankrupts is that a tax refund is similar to the vacation pay which was exempted from the Act in *Lines*. While there are some similarities, the critical question is whether the tax refund has those characteristics of vacation pay which were deemed pertinent to the Bankruptcy Act in *Lines*. The Supreme Court was concerned in *Lines* with the Act's purpose of enabling the bankrupt to make an "unencumbered fresh start." 400 U.S. at 20. The Court pointed out that the function of accrued vacation pay is "to support the basic requirements of life . . . during brief vacation periods or in the event of layoff." *Ibid.* The Court concluded that the bankrupt could not achieve the "new opportunity in life" which is a purpose of the Act if he must forego a vacation or take one without pay. The same simply cannot be said for an income tax refund. It is not a function

of the refund to support the basic requirements of life. That is the function of the bankrupt's regular wages. He does not forego future wages, after bankruptcy, because he loses his tax refund from previous wages. Even as to his past wages, at most he will typically lose from each week's payment a small fraction representing the excess withholding. Moreover, losing the refund is not the equivalent of foregoing a vacation or taking one without pay. Nor does it become so just because the bankrupt could elect to use the refund dollars for a vacation. By the same token he might like to use any funds he may have put aside prior to bankruptcy for a post-bankruptcy vacation, but the Act does not give him that choice.

Kokoszka also contends that some portion of his refund is immunized from the trustee by the restrictions on garnishment contained in the Consumer Credit Protection Act (CCPA), 15 U.S.C. §§ 1601 *et seq.* The restriction applies only to "disposable earnings," 15 U.S.C. § 1673, and that term is defined as "that part of the earnings of the individual remaining after the deduction from those earnings of any amounts required by law to be withheld." 15 U.S.C. § 1672(b). This definition precludes application of the CCPA to the amounts deducted in this case since all exemptions were claimed, even though it subsequently develops that some or all of those amounts are to be refunded.

In all three cases, the petitions for review are denied and the orders of the Referee are confirmed.

Dated at Hartford, Connecticut, this 21 day of July, 1972.

JON O. NEWMAN
United States District Judge

UNITED STATES DISTRICT COURT
DISTRICT OF CONNECTICUT

In Bankruptcy No. 36028

In the Matter of

HERBERT E. SANDS, BANKRUPT

In Bankruptcy No. 36197

In the Matter of

FRANK O'BRIEN, BANKRUPT

In Bankruptcy No. 37437

In the Matter of

HENRY A. KOKOSZKA, BANKRUPT

CLERK'S CERTIFICATE

I, GILBERT C. EARL, Clerk of the United States District Court for the District of Connecticut, do hereby certify that the foregoing copies of Docket Entries lettered, S.A., O.A., and K.A. and original papers numbered S1 through S8, 01 through 06, K1 through K7 and SOK 1 constitute the Record on these appeals.

And, pursuant to Rule 11(b) of the Federal Rules of Appellate Procedure, I further certify that this Record is transmitted to the Clerk of the Court of Appeals by certified mail this 13th day of October 1972.

Dated at Bridgeport, Connecticut, this 13th day of October 1972.

GILBERT C. EARL
Clerk

By: /s/ Thomas A. Grimes
THOMAS A. GRIMES
Deputy Clerk

[Filed United States Court of Appeals, Second Circuit Oct. 16, 1972, A. Daniel Fusaro, Clerk]

[SEAL]

IN THE
UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

[Title Omitted]

PETITION FOR ALLOWANCE OF APPEAL

* * * *

UNITED STATES COURT OF APPEALS
SECOND CIRCUIT

[Title Omitted]

* * * *

It is hereby ordered that the petition made herein by counsel for the appellants for allowance of appeal pursuant to Rule 6 of the Federal Rules of Appellate Procedure and Section 24 of the Bankruptcy Act (11 USC § 47) be and it hereby is granted.

/s/ Henry J. Friendly
HENRY J. FRIENDLY

/s/ J. EDWARD LUMBARD
J. EDWARD LUMBARD

/s/ Wilfred Feinberg
WILFRED FEINBERG
Circuit Judges

UNITED STATES COURT OF APPEALS
SECOND CIRCUIT

---

* * * *

[Title Omitted]

It is hereby ordered that the motion made herein by counsel for the appellants by notice of motion dated August 21, 1972, for leave to proceed in forma pauperis be and it hereby is granted.

/s/ Henry J. Friendly
HENRY J. FRIENDLY

/s/ J. EDWARD LUMBARD
J. EDWARD LUMBARD
Circuit Judges

/s/ Wilfred Feinberg
WILFRED FEINBERG

UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

(Argued February 28, 1973 Decided May 18, 1973.)

Docket No. 72-1972

In the Matters of

HENRY A. KOKOSZKA, FRANK O'BRIEN,
and HERBERT E. SANDS,
BANKRUPTS-PETITIONERS

Before:

KAUFMAN, ANDERSON and MANSFIELD,
Circuit Judges.

Appeal by petitioners in bankruptcy from judgment affirming orders of the referee, which held that an income tax refund is "property" which passes to the trustee under § 70(a)(5) of the Bankruptcy Act, 11 U.S.C. § 110(a)(5), in the United States District Court for the District of Connecticut, Jon O. Newman, *Judge.*

Affirmed in part; reversed in part.

STUART BEAR, Esq., New Haven, Conn. (William H. Clendenen, Jr., Esq., David M. Lesser, Esq., Joanne Faulkner, Esq., and Frank Dineen, Esq., New Haven, Conn., on the brief), *for Appellants.*

(RICHARD BELFORD, Esq., New Haven, Conn., on the brief, *for Appellee Trustee in Bankruptcy.*)

ANDERSON, *Circuit Judge:*

The three appellants herein each filed separate individual voluntary petitions in bankruptcy, all of which raise the issue of whether or not, and to what extent, an income tax refund passes to the trustee in bankruptcy as property of the estate. In each case the petitioner had claimed the maximum number of deductions to which he was entitled on his tax withholding statement and in each case the refund was the only asset of the bankrupt estate.

Henry Kokoszka filed his petition and was adjudicated a bankrupt on January 5, 1972. On February 3, the referee ordered him to turn over the proceeds of his 1971 income tax refund to the trustee. After a motion to vacate the order was denied, Kokoszka petitioned for review in the District Court. In the meantime, he turned over the refund amount of $250.90 to the trustee to hold pending the determination of this matter, and he was given his discharge in bankruptcy on August 24, 1972.

Herbert Sands was adjudicated a bankrupt on February 4, 1970 and was ordered to turn over his 1969 tax refund to the trustee. Instead, Sands spent his refund of $201.97, and the trustee moved on March 12, 1971, to deny the discharge for this reason. Subsequent to that, the petitioner moved to vacate the turn-over order, but the referee denied the motion and denied the discharge. Sands then petitioned the District Court for review.

Frank O'Brien was adjudicated a bankrupt on April 30, 1970, and was ordered to turn over his 1969 refund of $136.00 to the trustee. He, too, failed to obey the order and the trustee moved to deny the discharge on March 18, 1971. The referee has not yet ruled on the trustee's motion, but he did deny O'Brien's motion to vacate the original turn-over order, and the petitioner sought review of that denial.

After consolidating the three cases, the District Court held that the tax refunds were property that passed to the trustee under § 70(a)(5) of the Act, 11 U.S.C. § 110(a)(5), and that the Consumer Credit Protection Act, 15 U.S.C. § 1671, et seq., did not require that the trustee return 75% of the refund to the petitioners. On these issues we affirm; however, we do remand Sands' case in order that the referee may exercise his discretion on whether or not to grant him a discharge in bankruptcy.

The primary point raised by this appeal is whether or not a tax refund is "property" which passes to the bankruptcy trustee under § 70(a)(5) of the Act.[1] The Ninth Circuit recently held that such a tax refund is not § 70(a)(5) property, *In Re Cedor*, —— F.2d —— (9 Cir. Dec. 22, 1972); *aff'g on the opinion below*, 337 F. Supp. 1103 (N.D. Cal. 1972). *In Re Jones*, 337 F. Supp. 620 (D. Minn.) *leave to appeal denied* (8 Cir., May 14, 1971), *cert. denied*, 404 U.S. 1040 (1972), however, held that a refund does pass to the trustee and the same holding was implicit in *In Re Wetterhoff*, 453 F.2d 544 (8 Cir.), *cert. denied*, 409 U.S. 877 (1972), holding that, at the time of filing, the excess of accrued but unpaid wages over and above the portion exempt from attachment under state law, passed to the trustee.

The decision in the present case is governed in large part by two Supreme Court cases, *Segal* v. *Rochelle*, 382 U.S. 375 (1966), which held that a business generated

---

[1] The pertinent parts of § 70(a)(5) of the Bankruptcy Act, 11 U.S.C. § 110(a)(5), read as follows:

> "(a) The trustee of the estate of a bankrupt . . . [shall] be vested by operation of law with the title of the bankrupt as of the date of the filing of the petition initiating a proceeding under this title . . . to all of the following kinds of property wherever located . . . (5) property, including rights of action, which prior to the filing of the petition he could by any means have transferred or which might have been levied upon and sold under judicial process against him, or otherwise seized, impounded, or sequestered . . . ."

It is undisputed that the refunds could have been transferred under Connecticut law at the time of the filing of the petition, *cf.*, *Segal* v. *Rochelle*, 382 U.S. 375, 381-385 (1966).

loss-carryback tax refund, which did not accrue until after the filing of the bankruptcy petition, was § 70(a)(5) property, and *Lines* v. *Frederick*, 400 U.S. 18 (1970), which held that vacation pay, accrued but unpayable at the time of filing, did not pass to the trustee.

For the purpose of considering what treatment should be given to the tax refunds in question here, the term "property" in § 70(a)(5) must be defined in terms of the purposes of the Bankruptcy Act, rather than by more traditional concepts, *Segal*, *supra*, at 379; *In Re Spanish Language Television*, 456 F.2d 159, 162 (9 Cir. 1972). Basically, the term "property" is given a generous construction in order to give creditors everything of value, including items where the enjoyment of value is postponed, *Segal*, *supra*, at 379; *In Re Robbins Converting Corp.*, 441 F.2d 1096, 1098 (2 Cir. 1971). The definition of property is limited, however, where the debtors are wage earners "whose sole source of income, before and after bankruptcy, is their weekly earnings," *Lines*, *supra*, at p. 20, and who, at the filing of their petitions in bankruptcy have wages, as such, or as vacation pay, accrued but not yet paid, and where "the minimal requirements for the economic survival of the debtor are at stake," *id.*, such wage payments are not "property" to be turned over to the trustee under § 70(a)(5). The purpose of this exception is to give the debtor a "new opportunity in life and a clear field for future effort, unhampered by the pressure and discouragement of preexisting debt," *Lines*, *supra*, at 1-20; *Local Loan Co.* v. *Hunt*, 292 U.S. 234, 244 (1934).

The test as to whether or not such items as accrued but unpaid wages are or are not "property" to be turned over to the trustee is whether the item is "sufficiently rooted in the pre-bankruptcy past and so little entangled with the bankrupts' ability to make an unencumbered fresh start that it should be regarded as 'property' under § 70(a)(5)," *Segal*, *supra*, 382 U.S. at 380.

There were two petitioners in *Lines*, both of whom had accrued vacation pay at the time of the filing of the petition, but neither could receive it until he either went on vaction or his employment was terminated. The one

petitioner, Frederick, worked for a manufacturing company which shut down for a week twice a year thereby forcing their employees to take a vacation. The other, Harris, could choose his vacation period, if he desired to take one.

If the vacation pay was held to be property of the estate, it would appear at first glance that Harris was in a somewhat better position that Frederick, because Harris was not forced to take a vacation and go without basic support. Nevertheless, he also was in a difficult position. If he took a vacation, he would have no income for that period; yet, if he did not, and he was laid off, he would not have the use of the pay upon termination for basic support while seeking new work.

Realizing that "[t]he function of their accrued vacation pay is to support the basic requirements of life for them and their families during brief vacation periods or in the event of a layoff," the Supreme Court held that this vacation pay was a specialized type of property that did not pass to the trustee because to hold otherwise would deny the debtor the new opportunity in life which the Bankruptcy Act intended to provide, *Lines, supra*, at 20.

What we have then in *Lines* is a very narrow exception to the general proposition that everything of value passes to the trustee, i.e., vacation pay which will become essential for basic week to week support in the future does not pass. Because a tax refund is not the weekly or other periodic income required by a wage earner for his basic support, to deprive him of it will not hinder his ability to make a *fresh* start unhampered by the pressure of preexisting debt. Therefore, the tax refund is § 70 (a)(5) property which passes to the trustee.

The petitioners have advanced several arguments, however, that bear some comment. First, they maintain that wages, as such, are a specialized type of property which does not pass to the trustee and that a tax refund is nothing more than a refund of over withheld wages. The problem with this argument is that when the Court in *Lines, supra*, at 20, or in other cases such as *Sniadach* v. *Family Finance Corp.*, 395 U.S. 337 (1969), speaks

of wages as a special type of property, it is referring to the periodic payments required to meet basic needs.[2] Just because some property interest had its source in wages, however, does not give it special protection, for to do so would exempt from the bankrupt estate most of the property owned by many bankrupts, such as savings accounts and automobiles which had their origin in wages.

The petitioners also argue that as wage earners they have come to rely upon the tax refund as an expected annual event and that to take it from them would deny them a fresh start in life. It was this reasoning that convinced the court in *In Re Cedor*, *supra*, at 1105, that tax refunds should not be § 70(a)(5) property, but we find it unpersuasive. Many people may come to rely upon such things as a Christmas Club account or year end dividends from stock ownership to give them a special source of income at certain times of the year, but this does not make such items immune from a turn-over order in bankruptcy. Permitting a bankrupt to retain his tax refund would not be giving him a "fresh start" to accumulate new wealth but a "head start" over others who had no such refund.

Finally, the petitioners argue that a tax refund should not be § 70(a)(5) property because such refunds will often be of no benefit to the creditors but will be used up in administration expenses.

We are concerned with the fact that, on the average, in all personal bankruptcy cases 41% of the assets of the estates are paid out of for trustees' fees and other administration expenses, D. Stanley & M. Girth, Bankruptcy: Problem, Process, Reform 91 (Brookings Institution 1971). Furthermore, nearly one case in five is one of only nominal assets, that is, a case where all of the assets in the estate are consumed in administration expenses, leaving nothing for creditors, Stanley & Girth, *supra*, at 87-88, 175.

---

[2] We are fully aware that the petitioners in this case either spent or would spend their refunds for such needed items as health care, furniture and rent, but we do not see how the use of the money for what is characterized as "necessities" makes it any less § 70(a)(5) property, *cf.*, *Fuentes* v. *Shevin*, 407 U.S. 67, 90 (1972).

It is apparent why this happens in the small asset estates. Section 48(c)(1) of the Act, 11 U.S.C. § 76(c)(1), provides that a trustee can be compensated up to $150.00 plus expenses no matter how small the estate, and we have recently noted that in practice trustees are generally awarded the maximum fee, *In Re Schantz*, 390 F.2d 797, 800 (2 Cir. 1968); *see also*, Snedecor, Fees and Allowances in Straight Bankruptcy, 40 Ref. J. 26, 27 (1966). If that standard is applied to the cases currently before us, it can be seen that there will be nothing for creditors in the O'Brien estate and, at best, only a very small balance in the Kokoszka and Sands estates which might well be used up for other administration expenses, *cf.*, Stanley & Girth, *supra*, at 92, 173-195.

Clearly the purpose of the Bankruptcy Act was to benefit creditors and debtors, not trustees, *see*, *In Re Kingswood*, 343 F. Supp. 498, 504-05 (C.D. Cal.), *rev'd on other grounds*, —— F.2d —— (9 Cir. Dec. 22, 1972); *In Re Mc-Grath Mfg. Co.*, 95 F. Supp. 825, 829 (D. Neb. 1951). Therefore, there is no sense in taking a small sum from the bankrupt debtor, which he could well use to get started again, if there is to be no value to the creditors.

This does not mean, however, that all tax refunds should be held not to be § 70(a)(5) property, because a refund may be fairly large or only one asset among others. If a debtor is in a position where his non-exempt assets will be entirely eaten up by administration costs, leaving nothing for creditors, he can move the bankruptcy court for an order of abandonment,[3] *see In Re Mirsky*, 124 F.2d 1017 (2 Cir. 1942), *cert. denied*, 317 U.S. 638 (1942); *cf.*, *In re Ira Haupt & Co.*, 398 F.2d 607, 612-13 (2 Cir. 1968). See Calverley, Income Tax Refunds Due Wage Earners, 39 Ref. J. 8, 10-11 (1965), for a general discussion of the various abandoned practices of California referees for tax refunds. In moving for an abandonment, the debtor can present what evidence and

[3] A further benefit to a bankrupt debtor, if all assets are abandoned, is that a trustee need not be appointed which saves the petitioner $10 of the filing fee, *United States* v. *Kras*, —— U.S. —— (41 U.S.L.W. 4117, 4118, n. 2, Jan. 10, 1973).

arguments he may have to support his contention that it would not work an injustice to creditors to abandon the assets and not appoint a trustee. Whether or not to grant such a motion rests in the sound discretion of the Referee. He should grant the motion if it is reasonably clear that the assets, otherwise available for creditors, will be entirely consumed by trustee's fees and other administration expenses, that no creditor has shown that there was a likely opportunity for a trustee to recover additional assets, and that the absence of a trustee will not, under the circumstances, cast a substantial additional burden on the Bankruptcy Court.

The petitioners further argue, however, that even if a tax refund is § 70(a)(5) property, the trustee can take only 25% of it because of the Consumer Credit Protection Act's limitation on garnishment, 15 U.S.C. § 1671, et seq. That Act provides that no more than 25% of a person's aggregate disposable earnings for any workweek or other pay period may be subject to garnishment, 15 U.S.C. § 1673(a). The definitions of the key terms "earnings", "disposable earnings," and "garnishment" are set forth in the margin.[4]

The petitioners argue that a tax refund is "earnings" because it had its source in wages and that when it is returned to the taxpayer it is all "disposable earnings" because nothing is required by law to be withheld from the refund. Furthermore, they claim that the taking by the trustee is a "garnishment" because a bankruptcy pro-

---

[4] 15 U.S.C. § 1672 reads as follows:

"For the purposes of this subchapter:

(a) The term 'earnings' means compensation paid or payable for personal services, whether denominated as wages, salary, commission, bonus, or otherwise, and includes periodic payments pursuant to a pension or retirement program.

(b) The term 'disposable earnings' means that part of the earnings of any individual remaining after the deduction from those earnings of any amounts required by law to be withheld.

(c) The term 'garnishment' means any legal or equitable procedures through which the earnings of any individual are required to be withheld for payment of any debt."

ceeding is a legal or equitable procedure through which the earnings of an individual are withheld for payment of a debt.

Although this reasoning was adopted by the Ninth Circuit in *In Re Cedor, supra*, we do not follow it, but hold that a tax refund is not "earnings" for the purpose of § 1672 and, therefore, it is not protected by § 1673.

The intent of the Consumer Act was to make sure that wage earners were able to receive at least 75% of their take home pay in any one pay period so that they would have enough cash to meet basic needs. As a side effect, it was hoped that honest debtors, with this protection on their wages, would not be forced into bankruptcy, H. Rep. No. 1040, 90th Cong., 2d Sess., U.S. Code Cong. & Ad. News, 1962, 1977-79 (1968). It is clear, then, both from the language of the statute, §§ 1672, 1673, and the legislative intent, that "earnings" means periodic payments of compensation and does not pertain to every asset that is traceable in some way to such compensation. *See also*, 29 C.F.R. § 870.10(b): *In Re Kingswood, supra; cf. Lines, supra*, 400 U.S. at 20.

Petitioner Sands also appeals from the failure of the referee to exercise his discretion on whether or not to grant him a discharge in bankruptcy, even though he failed to obey the order to turn over his tax refund. The referee refused to consider a discharge, holding that § 14(c)(6) of the Bankruptcy Act, 11 U.S.C. § 32(c)(6),[5] mandated that he deny the discharge, if the bankrupt disobeyed a lawful order. The district court did not rule on the issue in this case, but in a similar case it remanded to the referee for him to exercise his discretion, *In Re Boudreau*, Bank. No. 36,601 (D. Conn. filed October 30, 1972).

Section 14(c) of the Act requires that a discharge be granted unless a bankrupt has done one of eight things,

---

[5] Section 14(c)(6) of the Bankruptcy Act, 11 U.S.C. § 32(c)(6) reads as follows:

> "(c) The court shall grant the discharge unless satisfied that the bankrupt has . . . (6) in the course of a proceeding under this title refused to obey any lawful order of, or to answer any material question approved by, the court; . . ."

among which is failure "to obey any lawful order of . . . the court," § 14(c)(6). The statute, however, does not state that a discharge *must* be denied for failing to obey an order, as the referee appears to have assumed.

As stated above, one of the primary purposes of the Bankruptcy Act is to give debtors a new chance in life and the various provisions of the Act must be read with this intent in mind, *Local Loan Co., supra*, 292 U.S. at 244-45; therefore Bankruptcy Courts must exercise their powers so that "substance will not give way to form" and "technical considerations will not prevent substantial justice from being done," *Pepper* v. *Litton*, 308 U.S. 295, 305 (1939). To this end, we have long held that the Act must be liberally applied toward the bankrupt applying for his discharge, *In Re Reisler*, 278 F. 618 (2 Cir. 1922); *see also, In Re Tabibian*, 289 F.2d 793, 795 (2 Cir. 1961).

Therefore the referee must exercise his discretion whether or not to grant a discharge, even when an order has not been followed. This position has strong support in the case law, *see, e.g. In Re Barbato*, 421 F.2d 1324, 1327 (3 Cir. 1970); *Jayne Meadows Travel Agency* v. *Dashiell*, 416 F.2d 1253, 1254 (9 Cir. 1969); *In Re Boudreau, supra; In Re Van Meter*, 208 F. Supp. 835 (S.D. Cal. 1962). The denial of a discharge can work a serious deprivation upon a debtor, and there are many circumstances where a bankrupt's disobedience may have been inadvertant or otherwise excusable. Moreover the denial of a discharge is not the only weapon available to the referee in order to enforce his orders as a recalcitrant petitioner can also be held in contempt, 11 U.S.C. § 69; *cf., In Re U. S. Hoffman Can Corp.*, 373 F.2d 622, 626 (3 Cir. 1967). This is not to be read, however, as minimizing the seriousness of the debtor's offense in disobeying a lawful order, nor do we suggest that a blatant violation should be condoned.

Therefore, before denying a discharge, the referee should weigh the detriment to the proceedings and the dignity of the court against the potential harm to the debtor if the discharge is denied. He should consider such factors as the intent behind the bankrupt's acts—

were they wilfull or was there a justifiable excuse; was there injury to the creditors; and is there some way that the bankrupt could make amends for his conduct. For example, in the present case, the referee might consider granting a discharge if the petitioner turns over to the trustee the amount of his refund check.

The decision of the District Court holding that the entire amount of the tax refunds is property belonging to the trustee in bankruptcy is affirmed; the case of petitioner Sands is remanded to the District Court for further proceedings consistent with this opinion.

UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

At a stated Term of the United States Court of Appeals for the Second Circuit, held at the United States Courthouse in the City of New York, on the eighteenth day of May one thousand nine hundred and seventy-three.

Present: HON. IRVING R. KAUFMAN
HON. ROBERT P. ANDERSON
HON. WALTER R. MANSFIELD
Circuit Judges

72-1972

In the Matter of
FRANK O'BRIEN, APPELLANT

In the Matter of
HENRY KOKOSZKA, APPELLANT

In the Matter of
HERBERT E. SANDS, APPELLANT

Appeal from the United States District Court
for the District of Connecticut

This cause came on to be heard on the transcript of record from the United States District Court for the District of Connecticut, and was argued by counsel.

ON CONSIDERATION WHEREOF, it is now hereby ordered, adjudged, and decreed that the judgment of said District Court be and it hereby is affirmed in part and reversed in part and that the action as to appellant Herbert E. Sands be and it hereby is remanded to said District Court for further proceedings in accordance with the opinion of this court.

A. DANIEL FUSARO
Clerk

UNITED STATES OF AMERICA
SOUTHERN DISTRICT OF NEW YORK

I, A. DANIEL FUSARO, Clerk of the United States Court of Appeals for the Second Circuit, do hereby certify that the foregoing documents, numbered from SA, S1-8, OA, O1-6, KA, K1-7, SOK1-2, I-VI, inclusive, comprise the original record certified by the Clerk of the United States District Court for the District of Connecticut and a transcript of the proceedings had in this Court in the case of

In the Matter of
Henry A. Kokoszka, Bankrupt

as the latter remain of record and on file in my office.

IN TESTIMONY WHEREOF, I have caused the seal of the said Court to be hereunto affixed, at the City of New York, in the Southern District of New York, in the Second [SEAL] Circuit, this twenty-third day of July in the year of our Lord one thousand nine hundred and seventy-three, and of the Independence of the said United States the one hundred and ninety-eighth.

A. DANIEL FUSARO
Clerk

by /s/ Vincent A. Carlin
Chief Deputy Clerk

SUPREME COURT OF THE UNITED STATES

No. 73-5265

HENRY A. KOKOSZKA, PETITIONER

v.

RICHARD BELFORD, TRUSTEE, ETC.

ON PETITION FOR WRIT OF CERTIORARI to the United States Court of Appeals for the Second Circuit.

ON CONSIDERATION of the motion for leave to proceed herein in forma pauperis and of the petition for writ of certiorari, it is ordered by this Court that the motion to proceed in forma pauperis be, and the same is hereby, granted; and that the petition for writ of certiorari be, and the same is hereby, granted.

December 10, 1973

☆ U. S. GOVERNMENT PRINTING OFFICE: 1974 529569 143

In the Supreme Court

OF THE

United States

OCTOBER TERM, 1973

No. 73-5265

HENRY A. KOKOSZKA, Bankrupt, *Petitioner,*

vs.

RICHARD BELFORD, Trustee in Bankruptcy of the Estate of Henry A. Kokoszka, Bankrupt, *Respondent.*

BRIEF OF AMICI CURIAE THE LEGAL AID SOCIETY OF SAN MATEO COUNTY, CALIFORNIA, AND HANSEN, JAFFE & WEISS, ATTORNEYS AT LAW IN SUPPORT OF THE PETITION FOR WRIT OF CERTIORARI

JOHN T. HANSEN,
MICHAEL H. WEISS,
HANSEN, JAFFE & WEISS,
555 Polk Street, Suite 201,
San Francisco, California 94102.
Telephone: (415) 771-5281.

THOMAS R. ADAMS,
LEGAL AID SOCIETY OF
SAN MATEO COUNTY,
6836 Mission Street,
Daly City, California 94014.
Telephone: (415) 994-1065,
Attorneys for Amici Curiae.

Subject Index

Table of Authorities Cited

Rules

Acts

Texts

In the Supreme Court
OF THE
United States

OCTOBER TERM, 1973

No. 73-5265

HENRY A. KOKOSZKA, Bankrupt, *Petitioner,*

vs.

RICHARD BELFORD, Trustee in Bankruptcy of the Estate of Henry A. Kokoszka, Bankrupt, *Respondent.*

BRIEF OF AMICI CURIAE THE LEGAL AID SOCIETY OF SAN MATEO COUNTY, CALIFORNIA, AND HANSEN, JAFFE & WEISS, ATTORNEYS AT LAW IN SUPPORT OF THE PETITION FOR WRIT OF CERTIORARI

I

INTEREST OF THE AMICI CURIAE*

The Legal Aid Society of San Mateo County is an OEO funded legal services program providing civil representation of poor persons in San Mateo County,

*Letters of consent from the petitioner and respondent to the filing of this brief pursuant to Rule 42(1) have been filed with the Clerk.

California. From its inception the Legal Aid Society has represented a substantial number of bankrupts and on account of that representation has a continuing interest in the administration of the Bankruptcy Courts.

Hansen, Jaffe & Weiss is a private law partnership specializing in the representation of wage earner bankrupts both for personal bankruptcies and for Chapter XIII arrangements. Thus Hansen, Jaffe & Weiss also has an ongoing interest in the administration of the Bankruptcy Courts.

Additionally, both the Legal Aid Society of San Mateo County and John Hansen and Michael Weiss of Hansen, Jaffe & Weiss represented the bankrupts in *Lines v. Frederick,* 400 U.S. 18 (1970), and in *Riggs v. James,* 470 F.2d 996 (C.A. 9 1972). In the case which is the subject of this brief, the United States Court of Appeals for the Second Circuit narrowly construed *Lines v. Frederick,* supra, and explicitly refused to follow *Riggs v. James,* supra.

II

ARGUMENT

A. INTRODUCTION

This case involves the question whether a refund owing to a bankrupt as the result of wage withholdings in excess of his or her tax liability should be treated as an asset of the bankrupt's estate.

The Court of Appeals for the Second Circuit, in the judgment entered hereinbelow, and the Ninth Cir-

cuit, in *Riggs v. James,* 470 F.2d 996 (C.A. 9 1972), *cert. denied,* 410 U.S. ___ (1973), have reached exactly opposite and conflicting conclusions with respect to this question.

The *Amici Curiae* herewith contend that the Ninth Circuit, in holding that such refunds are not to be treated as administratable assets, reached the correct conclusion, and that under the well-established "fresh start" doctrine a wage earner bankrupt should be entitled to retain and use such refunds received subsequent to filing bankruptcy.

B. THE TRADITIONAL VIEW OF BANKRUPTCY ADMINISTRATION SUPPORTS THE NINTH CIRCUIT'S CONCLUSION.

The administration of bankruptcy laws in non-business cases traditionally has been caught between the competing claims of creditors for the bankrupts' assets and of bankrupts' need for relief from the oppression of past debt. Thus, this Court has stated that the act of bankruptcy draws a "line of cleavage" across the bankrupts' life in an effort to resolve this conflict. Lovett v. Taylor, ~~*Andrews v. Partridge,*~~ 228 U.S. 474, 479 (1913). On the past side of the line the debtors' debts are discharged and his non-exempt assets mustered for his creditors. On the future side of the line the bankrupt gets a fresh start so that he may be a productive member of society and accumulate new assets without fear that they will be seized by his creditors. The latter consideration has become known as the "fresh start" doctrine. It has been stated and re-

affirmed by this Court time and again for almost a hundred years. *Neal v. Clark,* 95 U.S. 704, 709 (1877) (Opinion by Mr. Justice Harlan); *Traer v. Clews,* 115 U.S. 528, 541 (1885); *Wetmore v. Markoe,* 196 U.S. 68, 77 (1904); *Burlingham v. Crouse,* 228 U.S. 459, 473 (1913); ~~*Andrews v. Partridge,*~~ Everett v. Gordas supra; *Williams v. U. S. Fidelity and Guaranty Co.,* 236 U.S. 549, 554-55 (1915); *Stillwagen v. Clum,* 245 U.S. 605, 617 (1918); *Local Loan v. Hunt,* 292 U.S. 234, 244-45 (1934); *Lines v. Frederick,* 400 U.S. 18 (1970).

As the present case herein, this doctrine has been applied to personal bankruptcies. In *Local Loan v. Hunt,* supra, for example, the trustee attempted to use an Illinois wage lien law to reach across the "line of cleavage" to obtain for the creditors a bankrupt's wages after bankruptcy. Based on the "fresh start" doctrine, the Court held that in spite of the wage lien law the debtor's wages were his own after bankruptcy.

The more recent case of *Segal v. Rochelle,* 382 U.S. 375 (1966), however, presented unusual difficulties with respect to the application of the "fresh start" doctrine. In that case the trustee desired to reach forward across the imaginary "line of cleavage" to obtain a loss-carryback tax refund of a business bankrupt. Two circuit courts had ruled that the trustee could not reach such an asset. *In re Sussman,* 289 F.2d 76 (C.A. 3 1961); *Fournier v. Rosenblum,* 318 F.2d 525 (C.A. 1 1963). This Court acknowledged the difficulties *Segal* presented, *Segal* supra at 379, but noted that the case was different because a business bankruptcy was under consideration and because

of the peculiar nature of a loss carryback refund. Even with these critical distinctions, the Court conceded that *Segal* presented a close question. *Id.* at 378. Furthermore, as the Court emphasized in a later case, the "fresh start" doctrine was particularly inappropriate in *Segal* since the business had ceased to operate. *Lines v. Frederick,* 400 U.S. 18, at 20 supra.

Thus, *Segal* appears as an exceptional case along the landscape of the "fresh start" doctrine. The traditional approach emerged again in *Lines v. Frederick,* supra, where the Court held that the "fresh start" doctrine applied to prevent the trustee from reaching a wage earner bankrupt's accrued vacation pay.

In *Lines,* the same elements which had always before been important for application of the fresh start doctrine were present. The bankrupt was a wage earner. 400 U.S. at 18. The property in question was part of the bankrupt's wages. *Id.* at 20. The bankrupt's rights to his vacation pay arose after the date of bankruptcy, *Id.* at 18; see also, *Frederick v. Lines,* 425 F.2d 215, 216 (1970). Furthermore, in *Frederick v. Lines,* supra, the Ninth Circuit noted that its ruling would have little, if any, effect on creditors. *Id.* at 217.[1]

Because this case presents the issue of a refund derived from wages withheld for tax purposes, it superficially seems to have elements of both *Segal* and *Lines.* Nevertheless, District Judge Wollenberg in

[1]In fact in most non-business bankruptcies there are insufficient assets to pay any dividend to creditors. See *e.g.,* J. Lee, *Book Review,* 46 Am. Bankr. L. J. 159, 161 (1972); J. Dilenschneider, *Dischargeability, etc.,* 44 Ref. J. 83, n.2 (1970).

In re Cedor, 337 F.Supp. 1103 (N.D. Cal. 1972), demonstrated that upon close analysis the similarities to *Segal* are illusory.

> "Here the Court is confronted with elements of both *Segal* and *Lines*. The funds are received as a tax refund, but the refund is generated by the provisions of the Internal Revenue Code requiring certain amounts to be withheld from wages under *given* circumstances. In *Segal* the refund amounted to the recovery of a part of the taxes paid on profits in earlier years because of losses in the operation of a business in the taxable year; these losses also were a precipitating cause of the bankruptcy. In the instant cases, the Court is concerned with the refund of what was, in effect, a *forced* overpayment of tax on wages. There is nothing to suggest that the sums refunded were related to the circumstances which precipitated the bankruptcy. The Supreme Court considered the question in *Segal* to be 'close', 382 U.S. 379, 86 S.Ct. 511, 15 L.Ed. 2d 428; in light of *Lines* and *Snaidach* [sic], the balance on this question tips in favor of the bankrupt. The collection by the Internal Revenue Service without the consent or control of the bankrupt, and the belated refund, render these funds quite similar in a practical sense, to the accrued but unpaid wages which constituted vacation pay. If *Lines* stands for anything, it is that the practical realities are controlling in this determination." *In re Cedor,* 337 F.Supp. at 1105, supra.

In contrast the Second Circuit below stated:

> "What we have then in *Lines* is a very narrow exception to the general proposition that

> everything of value passes to the trustee, i.e., vacation pay which will become essential for basic week to week support in the future does not pass. Because a tax refund is not the weekly or other periodic income required by a wage earner for his basic support, to deprive him of it will not hinder his ability to make a *fresh* start unhampered by the pressure of existing debt." *In re Kokoszka* ..... F.2d ..... (C.A. 2 1973) (Slip Opinion p. 3674) [emphasis in the original].

The Second Circuit's analysis, unlike Judge Wollenberg's which the Ninth Circuit adopted, is based on false premises, *i.e.,* that *Lines* is an exceptional case. In fact, exactly the opposite is true: *Segal* is the exceptional case. The *Kokoszka* court cited no authority for its proposition that only property in the nature of periodic support is protected by the "fresh start" doctrine. Furthermore, to the extent the court's statement depends on factual matters in the record, it is erroneous. The record clearly shows that Kokoszka's tax refund check was necessary for his support. *In re Kokoszka,* ..... F.2d ..... (C.A. 2 1973) (Slip Opinion p. 3674). The *Kokoszka* court also failed to carefully analyze the "fresh start" doctrine in bankruptcy law. Its opinion permits a trustee to reach beyond the "line of cleavage" to seize a future refund derived from wages so that it may be applied to the burden of past debt. The *Kokoszka* court thus reached its conclusion without showing that any of the exceptional elements of *Segal* were present, contrary to the teaching of *Lines v. Frederick,* 400 U.S. 18, supra, as will be demonstrated below.

C. THE OPINION BELOW IS INCONSISTENT WITH LINES v. FREDERICK AND OTHER DECISIONS OF THIS COURT REGARDING A PERSON'S WAGES.

As discussed above, the result reached in *Riggs v. James,* supra, and *In re Cedor,* supra, reflected the important fact that the refunds in question represented the earnings of the bankrupts. *In re Cedor,* supra at 1105. In this regard the courts relied upon legal doctrines going back almost a hundred years. In *Traer v. Clews,* supra at 541, this Court said:

> "The policy of the bankrupt act was, after taking from the bankrupt all his property not exempt by law, to discharge from his debts and liabilities and enable him to take a fresh start. *His subsequent earnings were his own.*" [Emphasis added.]

The same important concept was reiterated in *Local Loan v. Hunt,* supra at 245.

> "The power of the individual to earn a living for himself and those dependent upon him is in the nature of a personal libery quite as much if not more than it is a property right."

This important concept was cited and relied upon in *Lines v. Frederick,* supra at 20. Nevertheless, the *Kokoszka* court erroneously suggests that *Lines* is out of the mainstream of decisional law and should not be relied upon to support the proposition urged herein. Moreover, *Lines* is also consistent with a number of recently decided and related non-bankruptcy decisions, which have considered the rights of wage earners. In each case, without exception, this Court

has protected the rights of the wage earner against the claims of the creditors.

The leading case is *Sniadach v. Family Finance Co.*, 395 U.S. 337 (1969)[2], which held that a person's wages may not be garnished without prior notice and hearing. *Sniadach* was followed by and cited as authority in *Lines* the following Term. 400 U.S. at 20. *Sniadach* and *Lines* were followed in a further series of cases favorable to wage earners. *E.g., James v. Strange,* 407 U.S. 128 (1972) [anti-exemption statute as to class of debtors held unconstitutional under 14th Amendment Equal Protection Clause]; *Fuentes v. Shevin,* 497 U.S. 67 (1972) [*Sniadach* applied to personal property as well as wages]; *Lynch v. Household Finance Co.,* 405 U.S. 538 (1972) [a person's right to enjoy and preserve property and wages is a basic civil right].

Consequently, the reliance of the Ninth Circuit in *Riggs v. James,* supra, upon *Lines v. Frederick,* supra, was not misplaced. Rather, *Lines,* a significant mainstream decision, is extremely apposite. This conclusion has been supported by the statement of one of the leading authorities on consumer bankruptcy law that the *Cedor* court's "extension of *Lines* does seem logical." Countryman, *The Use of State Law in Bankruptcy Cases I,* 47 N.Y.U. L. Rev. 407, 461 (June 1972).

---

[2]Critics of *Sniadach* also have tried to characterize it as an aberrational decision; but in *Fuentes v. Shevin,* 407 U.S. 67, 88 (1972), the Court took pains to point out that *Sniadach* is in the mainstream of its decisions.

Furthermore, the *Kokoszka* court's argument that property having its source in wages does not deserve special protection (Slip Opinion p. 3674) misconceives the case. At issue herein is not property purchased by wages or wages that have been otherwise disposed of; rather, the refund check is simply a return to the bankrupt of a forced overpayment of wages. *In re Cedor,* supra at 1105. Additionally both the factual record herein and reference to outside sources[3] demonstrates that the return of wages as a tax refund check is as necessary for the support of the bankrupt as his periodic wages or his vacation pay. Petitioner Kokoszka required his tax refund for otherwise deferred, but necessary medical expenses. *In re Kokoszka,* ..... F.2d ..... (C.A. 2 1973) (Slip Opinion p. 3674). Additionally as Mr. Justice Powell stated, speaking for a unanimous court in *James v. Strange,* 407 U.S. 128, 135:

> "The debtor's wages are his sustenance, with which he supports himself and his family. The average low income wage earner spends nearly nine-tenths of those wages for items of immediate consumption." [Footnote omitted.]

Such concern for wages seems especially important in the bankruptcy context because a bankrupt necessarily must look to the rewards of his labor for his fresh start.

---

[3]See Stanley & Girth, *Bankruptcy: Problem, Process, Reform,* 63 (Brookings Institution 1971).

D. THE RESULT OF THE HOLDING IN RIGGS v. JAMES IS NOT UNFAIR TO CREDITORS

As this Court in *Segal* looked also to the unfairness of depriving creditors of a loss-carryback refund, so too the Ninth Circuit in *Frederick v. Lines,* supra, observed that permitting bankrupts to retain their vacation pay will not adversely affect creditors. *Id.* at 217. In fact the Ninth Circuit noted the futility of a system which devours those very assets it was designed to collect when it stated:

> "[S]uch funds when, if ever, received by the employee would usually be consumed by the expenses of administration incurred to keep the estate open."

The Second Circuit also noted the same situation in the opinions below, as follows:

> "Clearly the purpose of the Bankruptcy Act was to benefit creditors and debtors not trustees [citations]. Therefore, there is no sense in taking a small sum from the bankrupt debtor, which he could well use." (Slip Opinion p. 3676).

A study of selected bankruptcies in the Northern District of California showed that the average dividend to unsecured creditors was less than seven-tenths of one per cent of scheduled indebtedness. *Riggs v. James,* supra, (Brief of Appellees, App. A). The same study shows that 64.3% of the assets marshalled went to pay administrative expense. *Id.* A study of eight other bankruptcy courts in the United States shows that 41% of all the assets mustered are consumed by administration, and that

the average dividend to unsecured creditors is 1.8%. D. Stanley and M. Girth, *Bankruptcy: Problem, Process, Reform,* 91 (Brookings Institution 1971).

Against these admittedly serious considerations, the *Kokoszka* court refers the bankrupt to the cumbersome and unlikely procedures of abandonment. Unfortunately such an alternative would only compound the present problem by placing additional burdens on the administration of the Bankruptcy Court, and create even greater lack of uniformity in the administration of the bankruptcy laws contrary to the express desires of the Congress in the Consumer Credit Protection Act. 15 U.S.C. §1671. Instead, it should be established uniformly that not only is a refund of wages from overpayment of taxes necessary for a bankrupt's fresh start, but also the loss of such an asset will rarely harm creditors.

E. THE RESTRICTIONS ON GARNISHMENT OF THE CONSUMER CREDIT PROTECTION ACT APPLY TO ANY PORTION OF THE REFUND CHECK THAT MAY PASS TO THE TRUSTEE.

The District Court in *Cedor* recognized the possibility of creating a forced savings fund through *voluntary* overwithholding and held that refunds attributable to such withholdings should pass to the trustee. The Court held, however, since such refunds are still wage payments that the restrictions on garnishment of the Consumer Credit Protection Act (hereinafter CCPA), 15 U.S.C. §§1671-77 are applicable to them. The Ninth Circuit also affirmed this

portion of the District Court's judgment. The court below, nevertheless, refused to follow that opinion and held to the contrary.

The fundamental provision of the CCPA prohibits garnishment of more than 25% of a person's disposable earnings. 15 U.S.C. §1673(a). Earnings are defined as follows:

> "Compensation paid or payable for personal services, whether denominated as wages, salary, commission, bonus or otherwise, and includes periodic payments pursuant to a pension or retirement program." 15 U.S.C. §1672(a).

There is no dispute that the refunds here consist entirely of compensation payable for personal services. The fact that in ordinary usage this compensation, when received, may be called a "tax refund check" should not affect its characterization since the Act broadly defines wages no matter how they are denominated. Moreover, the statute makes no distinction or exceptions that derive from the time of receipt; thus more delay in receipt in no way alters the characterization of the payment.

The court below, however, felt that earnings means "periodic payments of compensation." (Slip Opinion p. 3678). While it may be true that Congress could have so defined earnings if it had chosen to do so, a simple reference to the definition quoted above shows that Congress intended to include all "compensation paid or payable for personal services." Additionally, Congress specifically included, as examples of earnings, forms of compensation which are or may be

other than periodic payments such as bonuses and commissions. 15 U.S.C. §1672(a). As Judge Wollenberg succinctly stated in *In re Cedor,* supra at 1107:

> "There does not appear to be any reason of policy why the amount of the refund should be held to have lost its character as 'earnings' by reason of its somewhat circuitous route to the wage-earner's hand."

Since, however, the restrictions of the CCPA apply only to disposable earnings, the Court must analyze whether the refund check is disposable earnings. Disposable earnings are defined as follows:

> "That part of the earnings of any individual remaining after the deduction from these earnings of any amounts required by law to be withheld." 15 U.S.C. §1672(b).

The question is whether the amount required by law to be withheld is the amount the IRS ultimately withholds for the payment of the employee's tax liability. Such an interpretation appears to be in conformity with the purposes of the CCPA.

The purpose behind the definition of disposable earnings appears to be to permit creditors access to earnings of a wage earner only as they become available to him for spending—in this case when the refund check arrives. It is at this time—when the earnings become disposable—that the restrictions on garnishment apply, and the tax refund check becomes disposable only when received. Thus, the tax refund consists entirely of disposable earnings.

A "garnishment" is defined in the CCPA as:

> "[A]ny legal or equitable procedure through which the earnings of any individual are required to be withheld for the payment of any debt." 15 U.S.C. §1672(c).

The court below did not discuss the question of whether a garnishment had occurred in the case before it. However, the court did point out that on February 3, 1972, the bankruptcy Referee ordered Kokoszka to turn over to the trustee his 1971 tax refund check. *In re Kokoszka,* supra (Slip Opinion p. 3670).

There is no dispute here that the bankrupt's tax refund checks derived entirely from their earnings. Nor is there any dispute that these earnings are taken for payment of the debts listed in bankruptcy. Nor can it be disputed that the congressional definition of garnishment is broad and liberal. Nor can it be disputed that these refund checks are being withheld pursuant to the orders of the Bankruptcy Court. The orders of the Bankruptcy Court constitute "legal or equitable procedures" and thus a garnishment has occurred, and the restrictions of the CCPA should apply.

Finally, the Second Circuit's interpretation of this remedial statute is narrow and restrictive, contrary to accepted canons of construction. The court in *Cedor* correctly held that a remedial statute should be construed so as to carry out its intended purpose, rather than in a manner that frustrates that purpose. *In re Cedor,* 337 F.Supp. at 1107, supra. Under the rule

below the bankrupt loses entirely the exemption for a portion of his wages simply because its receipt by him was involuntarily postponed.

F. SUMMARY REVERSAL OF THE DECISION BELOW WOULD AID IN OBTAINING UNIFORM ADMINISTRATION OF BANKRUPTCY ESTATES THROUGHOUT THE UNITED STATES.

Over ninety percent (90%) of all bankruptcy proceedings presently filed nationwide are of a non-business nature, involving over-extended consumers who possess nominal estates. See, Schaeffer, *Proceedings in Bankruptcy in Forma Pauperis,* 69 COLUM. L. REV. 1203, 1210-12 (1969); and Dilenschneider, *Dischargeability: A Brief for the Consumer Bankrupt,* 44 REF. JOUR. 83 (1970). Consequently, questions involving refunds of excess withholdings undoubtedly arise frequently in bankruptcy courts throughout the country.

The decision of the Ninth Circuit in *Riggs v. James,* supra, is a correct, if not obvious, application of *Lines v. Fredericks.* The opinion of the court below to the contrary means that the bankruptcy laws now lack uniform application in a large circuit. Furthermore, the court below suggests that an opinion of the Eighth Circuit which does not even discuss these issues, by implication is also contrary to the rule of the Ninth Circuit. The present division not only causes an important lack of uniformity in the administration of personal bankruptcies, but it also presents difficult problems of administration for those courts without a Circuit decision.

In *Lines,* this Court summarily affirmed the judgment of the Ninth Circuit. In this case summary disposition reversing the court below and adopting the rule of the Ninth Circuit would be appropriate. Such a decision would not only achieve the constitutional goal of uniform administration of bankruptcy estates, but it would also promote the goal of the CCPA as stated in its preamble. 15 U.S.C. §1671(a).

III

CONCLUSION

For the reasons stated above *amici* urge the Court to grant the petition for writ of certiorari and summarily reverse the judgment of the court below and adopt the rule promulgated by the Ninth Circuit in *Riggs v. James,* 470 F.2d 996 (9th Cir. 1972).

Dated, 16 August 1973.

JOHN T. HANSEN,
MICHAEL H. WEISS,
HANSEN, JAFFE & WEISS,
THOMAS R. ADAMS,
LEGAL AID SOCIETY OF
SAN MATEO COUNTY,
Attorneys for Amici Curiae.

IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1973

No. 73-5265

HENRY A. KOKOSZKA, Bankrupt,

Petitioner

v.

RICHARD BELFORD, Trustee in Bankruptcy of the Estate of Henry A. Kokoszka, Bankrupt,

Respondent

ON WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

PETITIONER'S BRIEF

JOANNE S. FAULKNER
169 Church Street
New Haven, Connecticut

JOSEPH DEAN GARRISON, JR.
FREDERICK W. DANFORTH, JR.
THOMAS R. ADAMS
JOHN T. HANSEN
MICHAEL H. WEISS

Attorneys for Petitioner

Washington, D.C. • CLB PUBLISHERS, INC. • (202) 393-0625

TABLE OF CONTENTS

TABLE OF AUTHORITIES

Cases:

IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1973

No. 73-5265

HENRY A. KOKOSZKA, Bankrupt,

Petitioner

v.

RICHARD BELFORD, Trustee in Bankruptcy of the Estate of Henry A. Kokoszka, Bankrupt,

Respondent

ON WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

PETITIONER'S BRIEF

OPINIONS BELOW

The opinion of the Court of Appeals (App. 27) is reported at 479 F.2d 990. The opinions of the District Court for the District of Connecticut (App. 21) and of the Referee in Bankruptcy (App. 4) are unreported.

JURISDICTION

The judgment of the Court of Appeals for the Second Circuit was entered on May 18, 1973. Petition for writ of

certiorari was filed on August 10, 1973, within 90 days of the date of entry of the judgment. The jurisdiction of this Court rests on 28 U.S.C. Sec. 1254(1).

STATUTES INVOLVED

The statutory provisions involved herein are Bankruptcy Act Sec. 6, 11 U.S.C. Sec. 24; Bankruptcy Act, Sec. 70a, 11 U.S.C. Sec. 110a; and Consumer Credit Protection Act, 15 U.S.C. Sections 1671, 1672, 1673. The statutes are set forth in Appendix A.

QUESTIONS PRESENTED

1. Does a refund of wages involuntarily withheld from a wage-earning bankrupt in excess of his income tax liability become part of his bankruptcy estate as held by the court below, or is such a refund excluded from the purview of Sec. 70a of the Bankruptcy Act under the fresh start doctrine?

2. Assuming *arguendo* that some or all of the refund is property which vests in the trustee, does this refund of wage withholding receive the same exemption as to 75% thereof applicable to all other wage payments under the provisions of the Consumer Credit Protection Act, 15 U.S.C. Sec. 1671, *et seq.*?

STATEMENT OF THE CASE

Petitioner Henry A. Kokoszka had been employed for the first three months of 1971, was unemployed from April, 1971, to late December, 1971, and was re-employed for about the last week and a half of December, 1971. He received unemployment compensation during this long period without wages.

While employed, Mr. Kokoszka had two exemptions for federal income tax purposes and so advised his

employer. (App. 15). Accordingly, and pursuant to Internal Revenue Code withholding tables, the employer withheld an appropriate portion of his wages.

During the year 1971, Mr. Kokoszka's gross income was $2,322 (App. 19), which, under the tax laws, entitled him to a refund of the entire amount withheld, $250.90. It seems clear that this refund arose because the periodic withholdings from his pay were under a tax table geared to a full year's employment, which in fact did not occur.

Petitioner Henry A. Kokoszka filed his voluntary petition in bankruptcy on January 5, 1972. (App. 1, 15). The sole asset* claimed by the trustee in bankruptcy is a $250.90 refund of petitioner's wages, involuntarily withheld from earnings by his employer pursuant to the federal income tax laws.

On February 3, 1973, the referee in bankruptcy entered his customary *ex parte* order directing the bankrupt, when he received the refund, to turn it over to the trustee. (App. 2). On February 7, 1972, the bankrupt moved to vacate that order. (App. 3).

After hearing, the Referee found that Mr. Kokoszka needed a hernia operation or some form of abdominal support, dental work and eyeglasses. (App. 16). The Referee, however, denied Mr. Kokoszka's motion to vacate the turn-over order. (App. 11).

Kokoszka filed his tax return in mid-February, 1972. (App. 19). Some weeks later, when Mr. Kokoszka received his refund check, he complied with the order by turning it over to the trustee. The trustee is holding the money pending a determination as to whether or to what extent the refund is found to be property of the estate of the bankrupt.

The bankrupt next filed a Petition for Review of the Referee's decision with the District Court of Connecticut under Sec. 39c of the Bankruptcy Act, 11 U.S.C. Sec.

*The trustee abandoned as an asset a 1962 Corvair, upon bankrupt's payment of $25.

67c. The District Court affirmed the order of the Referee. (App. 21).

The bankrupt was granted leave to appeal, pursuant to Sec. 24a of the Bankruptcy Act, 11 U.S.C. Sec. 47a. On May 18, 1973, the Court of Appeals for the Second Circuit affirmed the order of the District Court as to the issues presented in this petition. It concluded: (1) that the tax refund is Sec. 70a(5) property which passes to the trustee; and (2) that the refund is not "earnings" within the Consumer Credit Protection Act and therefore not subject to the restrictions on garnishment.

SUMMARY OF ARGUMENT

A. The bankrupt contends that his income tax refund of $250.90 does not become Sec. 70a(5) property of the bankrupt estate under *Lines v. Frederick*, 400 U.S. 18 (1970). The judgment below is in conflict with *Lines v. Frederick*, and with a decision of the Ninth Circuit applying *Lines* to the same factual situation as exists herein. *In re James*, 470 F.2d 996 (9th Cir. 1972), *cert. den.*, 411 U.S. 973 (1973).

Although "the term 'property' has been construed most generously," for a wage earning bankrupt that term is limited by "the basic purpose of the Bankruptcy Act to give the debtor a 'new opportunity in life and a clear field for future effort, unhampered by the pressure and discouragement of preexisting debt.' " *Lines v. Frederick*, 400 U.S. at 19.

The principles of *Lines* are applicable here to protect bankrupt's tax refund from passing to the trustee, because the tax refund represents the bankrupt's wages, involuntarily withheld and not available to the bankrupt until some weeks after the date of filing. The bankrupt needed the refund to give him a fresh start in life, not one

handicapped by poor health, neglected because of inability to afford medical attention.

The judgment below is inconsistent with the mainstream of this Court's cases regarding the importance of a "fresh start" to a debtor, *e.g., Local Loan Co. v. Hunt*, 292 U.S. 234 (1934), and the importance of protection of a debtor's wages, *e.g., Sniadach v. Family Finance Corp.*, 395 U.S. 337 (1969).

The income tax refund has its sole source in wages and does not change its character as wages merely because it is called by another name. This Court regards wages as "a specialized type of property presenting distinct problems in our economic system". *Sniadach v. Family Finance Corp.*, 395 U.S. at 340. A "debtor's wages are his sustenance, with which he supports himself and his family." *James v. Strange*, 407 U.S. 128, 135 (1972).

The Court must also weigh other purposes of the Bankruptcy Act to decide if an asset is "property". Two of these purposes are to gather assets for the benefit of creditors, and to treat debtors uniformly across the nation. But, the vast majority of income tax refunds are small, and are used mainly to pay trustee's fees and other administrative costs, with little or no money trickling down to the creditor. Furthermore, the great variation in state exemption laws has produced nonuniform treatment of debtors due solely to the fortuity of their residence. A decision that the refunds do not become property would equalize the treatment of bankrupt wage earners.

Segal v. Rochelle, 382 U.S. 375 (1966) is not controlling here because it is factually distinguishable. The refunds there derived from a business tax loss carryover, not from wages. The Court's concern there was to benefit the creditors who had borne the burden of the losses; here the trustee would receive the benefit. *Segal* presented the Court with a close question, 382 U.S. at

379. This case, being more like *Lines*, requires a decision in favor of the wage earning bankrupt.

Accordingly, the Second Circuit was in error when it ruled that a bankrupt wage earner's income tax refund is property which passes to the trustee under Sec. 70a(5) of the Bankruptcy Act.

B. The bankrupt further contends that the restrictions on garnishment of the Consumer Credit Protection Act apply to the refund, if this Court determines that the refund is property which passes to the trustee.

Under the Consumer Credit Protection Act (CCPA), 15 U.S.C. Sec. 1673, 75% of an individual's disposable earnings are exempt from garnishment.

The refund here consists entirely of compensation payable for personal services, thus satisfying the broad definition of earnings in the CCPA. 15 U.S.C. Sec. 1672(a). Once the tax obligation has been determined, the amount refunded is disposable earnings, 75% of which are exempt from garnishment under the CCPA.

The trustee in bankruptcy takes title to property both as an attaching and executing creditor. Bankruptcy Act Sec. 70c, 11 U.S.C. 110c. The bankruptcy court's turnover order deprives the debtor of title to the refund; in fact, the Internal Revenue Service sometimes sends the refund directly to the trustee. This fulfills the definition of garnishment as "any legal or equitable procedure through which the earnings of any individual are required to be withheld for the payment of any debt". 15 U.S.C. Sec. 1672(c).

The U.S. Department of Labor, charged with administering the CCPA, has issued an opinion that the garnishment restrictions apply to all orders in bankruptcy except those Chapter XIII orders specifically exempted. Its construction is entitled to great weight. *Red Lion Broadcasting Co. v. FCC*, 395 U.S. 367, 381 (1969).

Accordingly, the Second Circuit Court of Appeals was incorrect in concluding that the Consumer Credit Protection Act does not exempt 75% of the income tax refund.

ARGUMENT

I.

BECAUSE IT DERIVES FROM WAGES, AND BECAUSE IT PROVIDES ONLY A MEAGER BENEFIT TO CREDITORS, A WAGE EARNER'S INCOME TAX REFUND, INVOLUNTARILY WITHHELD UNDER THE TAX LAWS, DOES NOT BECOME PROPERTY OF HIS BANKRUPTCY ESTATE.

This case involves the proper disposition of an income tax refund of $250.90 due to be received by a wage-earning bankrupt subsequent to filing bankruptcy. The issue is whether the refund, which is the sole asset claimed for the bankrupt's estate, is "property" as defined by Sec. 70(a) of the Bankruptcy Act.

Although Sec. 70(a) permits creditors to take bankrupts' non-exempt "property", the Act itself does not define "property". Consequently, this Court has observed that "the problem of classification for purposes of the Bankruptcy Act [cannot] be resolved simply by reference to the time when the right to the payment 'vested', or to definitions of property drawn from other areas of the law." *Lines v. Frederick*, 400 U.S. 18, 19 (1970). Rather, "The most important consideration limiting the breadth of the definition of 'property' lies in the basic purpose of the Bankruptcy Act to give the debtor a 'new opportunity in life and a clear field for future effort, unhampered by the pressure and discouragement of pre-existing debt' ". *Id.* at 20.

The rule thus restated in *Lines* has been imbedded in the bankruptcy law for nearly a century. *Segal v.*

Rochelle, 382 U.S. 375, 379 (1966); *Local Loan v. Hunt*, 292 U.S. 234, 245 (1934); *Williams v. U.S. Fidelity Co.*, 236 U.S. 549, 554-5 (1915); *Neal v. Clark*, 95 U.S. 704, 709 (1878); *Traer v. Clews*, 115 U.S. 528, 541 (1885).

The purpose of the Bankruptcy Act is to strike a balance between the interests of the debtor and the creditors. The balance here should tip in the bankrupt's favor, because a contrary result would be inconsistent with the Act's ultimate purposes. The "fresh start" which the Act gives a debtor is the basic reason the Act exists. Congress recognized that individuals can become trapped by a burden of debts they cannot pay. Such a burden not only ruins an individual's personal life, but can lead to counter-productive results such as the loss of a job. The policy allowing release from overwhelming debt is a realistic national policy which serves both the individual and society. REPORT OF THE COMMISSION ON BANKRUPTCY LAWS 87-94 (1973).

A. The Income Tax Refund Is a Wage Payment With the Same Characteristics as the Vacation Pay in *Lines v. Frederick*.

In *Lines v. Frederick*, 400 U.S. 18 (1970), this Court noted that vacation pay, involuntarily accumulated, accrued by a bankrupt wage earner at the date he filed his petition, but not payable until some future time, was part of his wages and was therefore deserving of special protection. It held that the accrued vacation pay did not become "property".

In this case, a fund of money involuntarily withheld from a bankrupt wage-earner, accrued at the date of the petition in bankruptcy, but not available until some future time, was held below to have lost its character as wages, and without that special protection became "property".

"Property" which passes to the trustee under Sec. 70a(5) of the Bankruptcy Act is limited where the debtor is a wage earner "whose sole source of income, before and after bankruptcy, is [his] weekly earnings", who has wages accrued but not payable at the time of bankruptcy. Because the function of wages "is to support the basic requirements of life", "the minimal requirements for the economic survival of the debtor are at stake". *Lines v. Frederick*, 400 U.S. at 20. Forcing the bankrupt to give up his wages is contrary to the purpose of the Bankruptcy Act to give the debtor a "new opportunity in life" and a " 'clear field for future effort, unhampered by the pressure and discouragement of pre-existing debt'." *Ibid.*

Lines and the instant case could hardly be more similar. In *Lines*, the following factors were present: (1) The vacation pay derived solely from the employment and wages of the bankrupt employees; (2) It was earned prior to the filing of the bankruptcy petitions; (3) It was accrued, unpaid and determinable at the time of filing the petitions; (4) The withholding of vacation pay by the employers was involuntary and outside the control of the bankrupts; (5) The fund was unavailable to the bankrupts until it actually became payable, *i.e.*, at the time of vacation or upon termination; (6) It was a planned-on, annually recurring payment, which entered into their families' anticipated annual budgets; (7) Its function was to meet their basic needs.

The wage earner tax refund has all of the above characteristics. In the case at bar: (1) the tax refund is derived solely from the employment and wages of the bankrupt employee; (2) It was earned prior to the filing of his bankruptcy petition; (3) It was accrued, unpaid and determinable at the time of the filing of his bankruptcy petition; (4) The withholding of wages for income taxes was involuntary, 26 U.S.C. Sec. 3402; (5) The tax refund is unavailable to the bankrupt until some

weeks after he has filed his tax return, 26 U.S.C. Sec. 6401 *et seq.*; (6) It is normally a planned-on annually-recurring payment entering into a bankrupt's annual spending budget; (7) Its function was to meet his basic needs, including long deferred medical care.

The function of the refund check was for basic support, exactly as wages are ordinarily used.[1] The court below recognized this (App. 32, n.2.), but found it legally immaterial since the refund was not a periodic wage payment. (App. 32).

That court interpreted *Lines* as being limited to "pay which will become essential for basic week to week support". *In re Kokoszka*, 479 F.2d 990, 994 (1973) (App. 31). That limitation did not exist, since either bankrupt in *Lines* could have terminated, accepted the pay and started a new job instead of taking time off. The Court's concern in *Lines* seemed to be with the "function" of wages as basic support,[2] rather than the use to which they would actually be put.

Speculation as to the actual use of deferred vacation pay and wages withheld for tax purposes is present in

---

[1] "The debtor's wages are his sustenance, with which he supports himself and his family. The average low income wage earner spends nearly nine-tenths of those wages for items of immediate consumption." *James v. Strange*, 407 U.S. 128, 135 (1972).

[2] A Brookings Institution study found that the items most commonly purchased by typical bankrupts immediately after a bankruptcy are a vehicle, an appliance, furniture, house and clothing in that order. Stanley & Girth, BANKRUPTCY: PROBLEM, PROCESS, REFORM, 63 (Brookings Inst. 1971).

The Bankruptcy Commission report shows that the median annual income of non-business bankrupts was in the upper $4,000.00 or lower $5,000.00 range. REPORT OF THE COMMISSION ON BANKRUPTCY LAWS, 54 (1973).

both *Lines* and *Kokoszka*. What is not speculation is that the use in both cases will be the same as wages regularly received, when received—for the necessities of life, as is the case for all low income wage earners.

The Second Circuit Court's emphasis on periodic wage payments as the only source of earnings needed to meet basic needs of life arises from a legal presumption it has drawn which is contrary to fact. *U.S. Dept. of Agriculture v. Murry*, 413 U.S. 508 (1973); *Vlandis v. Kline*, 412 U.S. 441 (1973). As one commentator has noted:

> "Some items which would qualify as basic requirements of life equal in importance to the ongoing expenses covered by vacation pay are not purchased on a weekly or monthly basis, and the annual tax refund may be relied upon to meet such requirements." Note, *The Income Tax Refund As A Possible Asset of A Wage Earner's Bankruptcy Estate*, 87 Harv. L. Rev. 395, 405 (1973).

If Kokoszka is deprived of his tax refund check, he could be forced to meet his required medical or other expenses by borrowing money which would be repaid on a monthly or similar basis. To thus force the bankrupt right back into debt hardly gives him the fresh start which is the purpose of the Act.

B. Since an Income Tax Refund is Part of the Bankrupt's Wages, it Deserves Special Protection.

For wage earner bankruptcies, one of the most critical and consistent concerns in application of the fresh start doctrine has been to protect the bankrupt from his creditor's claims on his subsequent earnings. This Court has recognized that the only opportunity most individual wage earners have to accumulate new wealth in the future

is from the wages they receive subsequent to bankruptcy. For example, in *Traer v. Clews*, 115 U.S. 528, 541 (1885), this Court said:

> "The policy of the bankrupt act was, after taking from the bankrupt all his property not exempt by law, to discharge from his debts and liabilities, and enable him to take a fresh start. His subsequent earnings were his own."

The same important concept was reiterated in *Local Loan Co. v. Hunt*, 292 U.S. 234, 245 (1934):

> "The power of the individual to earn a living for himself and those dependent upon him is in the nature of a personal liberty quite as much as, if not more than, it is a property right."

No decision of this Court has ever held that a form of personal earnings is property that passes to the creditors.

In this regard, moreover, the bankruptcy cases are only part of a larger legal picture, since wages have a special place in our legal system. Recent decisions only emphasize the fact that *Lines* is a mainstream decision of the law dealing with wages.

The leading case is *Sniadach v. Family Finance Corp.*, 395 U.S. 337 (1969), which held that a person's wages may not be garnished without prior notice and hearing. *Sniadach* was cited as authority in *Lines* the following term. 400 U.S. at 20. Both *Sniadach* and *Lines* were followed by a further series of cases recognizing the critical importance of wages to wage earners. *E.g.*, *James v. Strange*, 407 U.S. 128 (1972) [failure to give a class of debtors the same wage exemptions as others held unconstitutional under 14th Amendment Equal Protection Clause]; *Fuentes v. Shevin*, 407 U.S. 67 (1972) [*Sniadach* applied to personal property as well as wages because *Sniadach* was in the "mainstream of past cases". 407 U.S. at 88]; *Lynch v. Household Finance Corp.*, 405

U.S. 538 (1972) [a person's right to enjoy and preserve property and wages is a basic civil right].

The Second Circuit in the instant case attempted to evade the strong current of decisional law by claiming that the tax refund is not actually wages and thus undeserving of special protection. (App. 32). The court there compared the annual event of the tax refund (without distinguishing between voluntary and involuntary withholding) to a "Christmas Club account or year end dividends". (App. 32). This analogy fails since the wage withholding here is involuntary, not an intentional use of the money. Other examples given by the Second Circuit as property having its source in wages are within a bankrupt's control. (Indeed, he may always sell his stocks, dispose of bank accounts, or not choose, or be in a position, to save at all.) A voluntary fund can be liquidated if it is necessary to provide for basic support. Mr. Kokoszka's case is instructive because surely he needed his involuntarily withheld wages for basic support, which in his case included critical medical needs. A voluntary savings plan of any sort was clearly out of the question, and in fact was not the case here.

The artificiality of the lower court's attempt to identify the refund as a property interest rather than wages is further demonstrated by the facts and policy underlying the withholding sections of the Internal Revenue Code.

The Code requires a wage earner to fill out a withholding exemption certificate for his employer. 26 U.S.C. Sec. 3402(f)(2)(A). The employer then withholds a portion of the employee's wages, calculated according to certain tables, to cover estimated federal income taxes. 26 U.S.C. Sec. 3402(a). Thus the policy of the withholding system compels each employee to prepay part of his wages as an approximation for the tax due after year's end. For various reasons, this approximation may be in

excess, and the United States must return a certain amount of the wages it has withheld.

Because the bankrupt here was compelled for reasons of national policy[3] to involuntarily accumulate part of his wages in anticipation of taxes should not change the nature of the money involved. Nor should the common description of the money as a "tax refund check" affect the fact that it is wages. The *Cedor* court more accurately termed the refund check as "a *forced* overpayment of tax *on wages*". 337 F. Supp. at 1105. It concluded that "there does not appear to be any reason of policy why the amount of the refund should be held to have lost its character as earnings by reason of its somewhat circuitous route to the wage earner's hand". *Id.* at 1107. Se also *In re Freedomland*, 480 F.2d 184, 190 (2d Cir. 1973), *cert. granted sub nom. Otte v. U.S.*, Jan. 21, 1974, where the court said in another bankruptcy context, "Conceptually the [withholding] tax payments should be treated in the same way as the wages from which they derive and of which they are a part".

C. The Principles of *Lines v. Frederick* Govern the Disposition of a Bankrupt's Tax Refund Check Because a Contrary Result Will Not Benefit Creditors.

Like the bankrupt here, most wage earners who are forced into straight bankruptcy have little or no assets

---

[3] The court in *Cedor* stated that:

"It is the national interest, according to the provisions of the Internal Revenue Code, to have taxpayers make certain that enough is withheld, so that taxes are promptly paid. The taxpayer is encouraged to err on the side of over-withholding. A decision here that all excess withholding must go to the trustee in bankruptcy would certainly tend to frustrate the objective of the withholding laws." *In re Cedor*, 337 F. Supp. 1103, 1107 (N.D. Cal. 1972), *aff'd sub nom. In re James*, 470 F.2d 996 (9th Cir. 1972), *cert. den.* 411 U.S. 973 (1973).

that are of any value to creditors.[4] *Perry v. Commerce Loan Co.*, 383 U.S. 392, 396 (1966). Why are so few assets available? Professor Charles Seligson, in analyzing bankruptcy cases closed in 1967 and 1968, concluded that:

> "[T]he proceedings were initiated too late, that is after substantially all of the assets of the bankrupts had been dissipated. It must be recognized that most debtors, both in business and non-business, will exert every effort to avoid bankruptcy. Debtors never seem to give up hope that help is just around the corner. To most of society, bankruptcy is an evil word quite often associated with immorality. It is not surprising, therefore, that bankruptcy as an instrument of relief from financial pressures is availed of generally only *in extremis.*" *Major Problems For Consideration By The Commission on Bankruptcy Laws Of The United States*, 45 Am. Bankr. L. J. 73, 86 (1971).

A nationwide, selected survey presents a compelling statistical picture. The data shows that the average

---

[4]The average non-business bankrupt owed $5,000 to 12 creditors, mainly finance companies, retail merchants and banks. Stanley & Girth, *op. cit. supra* at 57. The great majority of straight bankruptcies are no-asset cases (70%); a small amount are nominal asset cases (15%) and 15% are asset cases. A Referee in Bankruptcy has concluded that "the more common variety of consumer bankruptcy case is that which is initiated long after the debtor's financial circumstances have fallen into hopeless decline. No realistic prospects for asset recoveries . . . remain. . . . Virtually all of the debtor's non-exempt, unencumbered property is either valueless or has been attached or repossessed long before bankruptcy". Cyr, *Single Claim Jurisdiction*, 46 Am. Bankr. L.J. 199, 226 (1972). Cf. Stanley and Girth, BANKRUPTCY: PROBLEM, PROCESS, REFORM 47, 48 (Brookings Inst. 1971).

dividend to creditors is equal to only seven-tenths of one percent (0.7%) of the unsecured indebtedness.[5]

A similar survey was done in the Northern District of California by the attorneys for the bankrupts in *In re James*, 470 F.2d 996 (9th Cir. 1972). (Brief of Appellees, Appendix A). That study also shows that the dividend to unsecured creditors was less than one percent of scheduled indebtedness.

The bankrupt's case here is the same. Kokoszka's total scheduled unsecured indebtedness is $6,105.22 and his tax refund check is $250.90. The record does not reveal the amount which would be deducted for payment to the trustee and for administration expenses, but the Court below noted that there might be only a very small balance in the Kokoszka estate. *In re Kokoszka*, 479 F.2d 990, 995 (1973) (App. 33).

Similar facts regarding vacation pay caused the Ninth Circuit to note that allowing bankrupts to retain their vacation pay would only rarely harm creditors. *Frederick v. Lines*, 425 F.2d 215, 217 (9th Cir. 1970), *aff'd* 400 U.S. 18 (1970).

---

[5] Stanley & Girth, *op. cit. supra* at 90-93 and 232-33. This figure is extrapolated from their data. At page 93 they state that the average dividend to unsecured creditors whose claims were approved and allowed was seven percent (7%), but on page 90 it appears that only ten percent (10%) of unsecured creditors bother to file claims primarily because they have learned that the process is unrewarding. In Appendix B at page 232-33 the authors estimate that the total liabilities of all bankrupts in 1968 was $2,168 million and that creditors received $182 million or nine-tenths of one percent (0.9%). Of course, this includes secured and priority creditors whose percentage return is slightly higher than that of unsecured creditors. *Id.* at 92-3. Thus the seven-tenths of one percent (0.7%) figure seems to be a reasonable estimate based on the raw data.

Income tax refunds, like vacation pay, generally involve small amounts. Two-thirds of all the refunds in one survey were for amounts less than $200.00, and no refund in its sample exceeded $1,000.00; Stanley & Girth, BANKRUPTCY: PROBLEM, PROCESS, REFORM 85 (Brookings Inst. 1971). (Indeed only twelve percent (12%) of the personal bankrupts in the study had to turn over refunds to the trustee. *Ibid.*)[6]

Thus, what happens is that a substantial portion of the assets collected in non-business bankruptcies goes to the very persons who have been appointed to act for the creditors. Stanley & Girth, *op. cit. supra*, found that "41% of the assets of these estates are paid out for trustees' fees and other administration expenses". *In re Kokoszka*, 479 F.2d at 995 (App. 32). In the *In re James* survey, *supra*, the trustees (and their attorneys) consumed fifty-five percent (55%) of the assets collected. Another nine percent (9%) of the assets was consumed by administration expenses.

The Ninth Circuit noted the irony that such assets are consumed by the expenses of administration incurred to obtain the asset. *Frederick v. Lines*, 425 F.2d at 217. The Second Circuit also condemned such a result, stating: "Clearly the purpose of the Bankruptcy Act was to

---

[6] Referee Seidman of the District of Connecticut has commented:

> "In the case of a consumer-bankrupt, a potential tax refund covering an overpayment of withholding taxes during the current year *and* wages unpaid at the date of filing *at best* would provide minimal assets to the estate. There is little likelihood of any significant benefit to creditors as there might be in the case of tax loss carry-back of a business bankrupt." [Emphasis added.]

Seidman, *Some Implications of Segal v. Rochelle*, 40 Ref. J. 107, 109 (1967).

benefit creditors and debtors, not trustees." *In re Kokoszka*, 479 F.2d at 995-96 (App. 33).

Against this background of the overwhelming majority of cases, the argument can be made that in an occasional case refunds are large enough, either alone or in combination with other assets, to provide a substantial dividend to creditors. The solution proposed below, *i.e.*, to petition the referee for abandonment of small refunds, adds to the cost and time involved in administration, and involves the exercise of discretion which would undoubtedly erode further the uniformity of the administration of bankruptcy. REPORT OF THE COMMISSION ON BANKRUPTCY LAWS at 122-23 and 15 U.S.C. Sec. 1671(a)(3). It is additionally noteworthy that there has been no abandonment in the case at bar.

At issue herein are the "practical realities", *In re Cedor*, 337 F. Supp. at 1105, in a federal law which should be uniformly stated rather than allocated to the inevitably disparate results of referee discretion.

D. A Decision Exempting an Income Tax Refund From the Assets of the Bankrupt's Estate Does Not Result in a "Head Start" for Some Bankrupts, But Instead it Encourages the Exemplary Goal of Uniform Treatment of all Bankrupts.

The court below cited an obscure phrase in a dissenting opinion by Mr. Justice Harlan in *Lines* when it stated that allowing the bankrupt to exempt his refund from the creditors' claims would provide him with a "head start[7] over others who had no such refund". *In re Kokoszka*, 479 F.2d 990, 995 (App 32).

---

[7]In using the phrase "head start", Mr. Justice Harlan was not referring to a head start over other bankrupts. He seemed to refer instead to a head start over a nonbankrupt who started to work on

The fact that one bankrupt may leave bankruptcy with more assets than another seems legally irrelevant. A bankrupt may retain a tort recovery, or an expected inheritance or gift, which would leave that bankrupt with more assets than another. *Segal v. Rochelle*, 382 U.S. 375, 379 (1966); Bankruptcy Act, Sec. 70a(5), 11 U.S.C. Sec. 110a(5). Nowhere in the Bankruptcy Act is such a result prohibited.

Furthermore, state exemptions vary widely. "[S]tate laws governing exemptions are not fair because of the great variations among them, leading sometimes to abuse and at other times to undue hardships. . . ." Enzer, de Brigard & Lazar, SOME CONSIDERATIONS CONCERNING BANKRUPTCY REFORM 11 (Inst. for the Future, 1973).

> "[T]he treatment of exemptions is characterized by both inequities and waste motion. . . . The inequities are largely due to the often obsolete and extremely diverse provisions of state exemption laws." Stanley & Girth, BANKRUPTCY: PROBLEM, PROCESS, REFORM 81 (Brookings Inst. 1971).

See also REPORT OF THE COMMISSION ON BANKRUPTCY LAWS 22, 180 (1973).

Thus, some states have a homestead exemption;[8] Connecticut does not. Some states exempt wages en-

---

the date of Mr. Frederick's bankruptcy. The "head start" arose from the state exemption of one half of the pay accrued within 30 days prior to filing the petition, which thus allowed Mr. Frederick to retain a half day's credit of vacation pay. The reverse is true here, since a nonbankrupt would have the benefit of his refund while the bankrupt would not.

[8] Texas' homestead exemption law allowed Ernest Medders to keep 200 acres of land, a $250,000 house, and a $175,000 "party barn". Note, 53 Corn. L. Rev. 663, 665 (1968).

tirely; others "exempt only a ridiculously low set amount"; Connecticut has no such exemption (unless one is provided by the Consumer Credit Protection Act, as the bankrupt argues in Part II hereof.) Cowan, BANKRUPTCY LAW & PRACT. Sec. 630.

It is clear that income tax refunds are treated in this varying manner:

> "Local attitudes affected the practice concerning the collection of tax refunds. None of the cases in Northern Alabama showed this type of asset. Some (though not all) referees in Southern California read a statutory provision giving them discretion to pay trustees up to $150 from the available assets of the estate as permitting them not to collect tax refunds under that amount. . . . Elsewhere, the tax refund was often the only source of compensation for the trustee." Stanley & Girth, *op. cit. supra* at 85-86.

A referee in California confirms that:

> "No doubt, the policy with regard to abandonment of income tax refunds because of the small amount involved varies throughout the country in considerable degree. It varies considerably even in this District. . . . I think it is too much to expect uniformity on this policy of abandonment because of the different conditions which exist in different Districts and different localities within a District." Calverley, *Income Tax Refunds Due Wage Earners*, 39 Ref. J. 8, 10 (1965).

Some referees allow the abandonment of refunds under $150. Snedecor, *Fees and Allowances in Straight Bankruptcy*, 40 Ref. J. 26, 27 (1966); *In re McKenzie*, No. 22635-B-4 (D. Kan. 1972).

In Ohio, an income tax refund of less than $500 is exempt where the bankrupt has no homestead, under a state exemption statute. *In re Perry*, 225 F. Supp. 481 (N.D. Ohio 1963).

In the Ninth Circuit, the income tax refund does not vest in the trustee, except insofar as it results from voluntary withholding. *In re James*, 470 F.2d 996 (1972). Of the voluntary withholding, only 25% vests in the trustee. In the Second Circuit, the refund vests in the trustee. *In re Kokoszka*, 479 F.2d 990 (1973).

Most inequitable of all, "Debtors who are carefully advised and who can wait do not file in bankruptcy until tax refunds have been cashed and spent. . . ." Stanley & Girth *op. cit. supra* at 85. Kokoszka could not wait. Nor did he live in a jurisdiction where his refund would be exempt or abandoned. Compared with other bankrupts, then, Kokoszka does not have a "head start" even if he is allowed to keep the refund.

It is possible that Mr. Justice Harlan or the Second Circuit Court may have linked the phrase "head start" to some fundamental issue of fairness. If so, the question of fairness deserves to be analyzed rather than be cast aside by a quick phrase. The record here reveals that the bankrupt needed his tax refund check for medical expenses which were deferred on account of his pre-bankruptcy financial condition. Because the refund is derived entirely from a forced withholding of wages, there are none of the problems of fairness that troubled this Court about the loss carryback refund in *Segal*. For the bankruptcy court to take an "asset" which the bankrupt was forced by law to accumulate, rather than use for subsistence, is unduly oppressive to the bankrupt.

The commentators have written that the collection of these tax refund checks "are cruel to the bankrupt and productive of costly paperwork". Stanley & Girth, *op. cit. supra* at 86. They recommend a nationwide and uniform exemption law, to produce the most equitable results. Enzer, de Brigard & Lazar, *op. cit. supra* at 11; Stanley & Girth, *op. cit. supra* at 5.

Lastly, the creditor community can derive benefit from a uniform rule of law:

> "Especially from creditors' perspectives, it is important to have rules that determine rights generally in the debtor's wealth wherever situated, and thus guide conduct in the open credit economy, as well as collective processes which effect such rules and permit creditors to realize on their claims." REPORT OF THE COMMISSION ON BANKRUPTCY LAWS 84 (1973).

The Ninth Circuit decision in *In re James* establishes a uniform rule of law, thus determining rights in a manner that might guide creditor conduct in a multistate credit economy. A contrary decision which may allow some creditors to receive a few cents on the dollar, cannot guide creditors and is needlessly cruel to debtors.[9]

E. A Wage Earning Bankrupt's Tax Refund Check is not Like the Tax Loss Carryover in *Segal v. Rochelle.*

In *Segal v. Rochelle*, 382 U.S. 375 (1966), this Court noted that two, sometimes competing, purposes of the Bankruptcy Act are to give a debtor a fresh start and to distribute assets to the bankrupt's creditors. *Segal v. Rochelle*, 382 U.S. at 379. The balance in *Segal* was

---

[9] Referee Calverley also noted that there is considerable delay either in getting information from the I.R.S. or in securing the refund check. Even if the time for filing objections to the discharge has expired, a discharge can be reopened and denied if the refund is not turned over to the trustee. Calverley, *Income Tax Refunds Due Wage Earners*, 39 Ref. J. 8, 10, 11 (1965). This procedure seems administratively very costly, extremely cruel to the bankrupt, with benefit running mainly to the trustee in a fee to compensate for his time.

tipped in favor of the creditors because the bankrupts would be discouraged from earning if the loss carryback refund were available to them, and because it seemed unfair to reimburse the bankrupt for business losses which his creditors had been forced to bear.

Yet, the Second Circuit chose to regard a wage earner's refund as analogous to the loss-carryback tax refund of a business bankrupt in *Segal v. Rochelle*, rather than to the accrued vacation pay of the wage earners in *Lines*. Close analysis reveals that the *only* similarity between *Segal* and *Kokoszka* is that both involve money returned to a bankrupt by the Internal Revenue Service.

Segal involved a business bankrupt, not a wage earner. The Court in *Segal* was not particularly concerned with the fresh start doctrine, because the tax loss carryback refund belonged to "a business [that] has ceased to operate". *Lines v. Frederick*, 400 U.S. at 19. Here we have an individual wage earner, as in *Lines*, who survives the bankruptcy and needs whatever income comes to him thereafter for his fresh start.

Thus, *Segal* stands for little more than the proposition that the fresh start concept did not apply to its unique facts; indeed it emerges as the exception along the landscape of fresh start cases decided by this Court.

Furthermore, the nature of the loss carryback refund (a "very special situation", *In re Sussman*, 289 F.2d 76, 78 (3d Cir. 1961)) raised unusual problems of fairness. A loss carryback refund would have reimbursed the business for losses it sustained in previous years. However, upon bankruptcy, the business no longer sustained the losses; they were passed on to its creditors. Thus fairness required that any payment for those losses also be passed on to the creditors. With a wage earner, an income tax refund is the result of an involuntary approximation of taxes owing. No money is paid to the wage-earning

bankrupt for his economic losses which are now borne by his creditors. The only payments a personal bankrupt might receive that could be construed as government reimbursement for such losses are workmen's compensation or unemployment insurance. *Segal* does not apply to such payments. The logic of *Segal* is simply inapplicable to income tax refunds.

There are other distinctions between *Segal* and the instant case. The wage-earner, practically speaking, can expect a tax refund "as an annual event", *In re Cedor*, 337 F. Supp. at 1105, especially if, as in Mr. Kokoszka's case, he is unemployed, sick or otherwise unable to work for part of a year. In terms of a "fresh start", deprivation of this fund is not any less severe than deprivation of vacation pay, since both losses may lead to some period of future support at an income level lower than that which would cover basic needs. Similarly, families may rely on the receipt of these funds and defer the purchase of necessities until the expected receipt. In contrast, the tax loss carry-back in *Segal* would have resulted in a significant windfall to the Segals personally, since the business which generated the losses had dissolved.

The relationship of both *Segal* and *Lines* to a wage earner bankrupt's tax refund check was correctly analyzed by District Court Judge Albert Wollenberg, *In re Cedor*, 337 F. Supp. 1103, 1105 (N.D. Cal. 1972).

> "Here the Court is confronted with elements of both *Segal* and *Lines*. The funds are received as a tax refund, but the refund is generated by the provisions of the Internal Revenue Code requiring certain amounts to be withheld from wages under given circumstances. In *Segal* the refund amounted to the recovery of a part of the taxes paid on profits in earlier years because of losses in the operation of a business in the taxable year; these losses also were a precipitating cause of the bankruptcy.

In the instant cases, the Court is concerned with the refund of what was, in effect, a *forced* overpayment of tax *on wages*. There is nothing to suggest that the sums refunded were related to the circumstances which precipitated the bankruptcy. The Supreme Court considered the question in *Segal* to be 'close', 382 U.S. 379, 86 S.Ct. 511, 15 L.Ed.2d 428; in light of *Lines* and *Snaidach* [sic], the balance on this question tips in favor of the bankrupt. The collection by the Internal Revenue Service without the consent or control of the bankrupt, and the belated refund, render these funds quite similar in a practical sense, to the accrued but unpaid wages which constituted vacation pay. If *Lines* stands for anything, it is that the practical realities are controlling in this determination."

The *Cedor* opinion has received the support of leading academic commentators. Note, *The Income Tax Refund as a Possible Asset of a Wage Earner's Bankruptcy Estate*, 87 Harv. L. Rev. 395 (1973); Countryman, *The Use of State Law in Bankruptcy Cases I*, 47 N.Y.U.L. Rev. 407, 461 (1972). As the Harvard Law Review commentator said:

"The characteristics of refunds resulting from mandatory overwithholding present a more compelling case for retention by the bankrupt than loss-carryback refunds in that their ties to the past are less clear, their importance for an individual's fresh start is more evident, and their status as a form of compensation to a wage earner is such as to require greater protection than that afforded business-related refunds." 87 Harv. L. Rev. at 406.

A secondary test in *Segal* was whether the fund was "sufficiently rooted in the pre-bankruptcy past". 382 U.S. at 380. In *Segal* a true "tax" refund was available,

because the refund was from taxes already paid on business profits in earlier years. Mr. Kokoszka's refund was no more than a wage refund because a tax liability never arose.

Furthermore, a tax refund can accrue to a wage-earner not only from the loss of a job before filing a petition, but also from events which may follow a petition, such as marriage or the birth of a child. Thus, a wage-earner's tax refund is not rooted in the past, but is often contingent on events future to the date of filing the bankruptcy petition.

When a wage-earner files a bankruptcy petition, the court's duty is "to secure for creditors everything of value the bankrupt may possess in alienable or leviable form *when he files his petition*" and "to leave the bankrupt free *after the date of his petition* to accumulate new wealth in the future." *Segal v. Rochelle, supra* at 379 (Emphasis added.) Thus the filing date draws a "line of cleavage" across the bankrupt's life. *Everett v. Judson*, 228 U.S. 474, 479 (1913).

A recent comment suggests that although the "line of cleavage" argument has not been "wholly dispositive" of past cases,[10] that a:

---

[10]In *In re Aveni*, 458 F.2d 972 (6th Cir.) *cert. den.*, 409 U.S. 877 (1972), the Sixth Circuit held that non-exempt wages, recently accrued, presently owing and payable substantially current with bankruptcy are property. *Aveni* dealt with a different question from this case, and in fact affirmed that wages the bankrupt cannot collect until some date subsequent to the bankruptcy do not pass to the trustee. *Id.* at 973. It concluded, however, that non-exempt wages immediately payable are an exception to *Lines* because: (1) the receipt of the wages is virtually contemporaneous with the bankruptcy proceedings and (2) the bankrupt's ability to make a fresh start was not threatened, especially since he was able to claim the very substantial exemption against garnishment allowed by state law.

"Modification of the past-future distinction to focus on *time of payment* rather than date of earning supports the treatment of refunds resulting from mandatory withholding as 'future earnings' when they will not be received until a number of weeks after the date of filing. Such refunds are generally less accessible to a bankrupt at the time of filing than was the vacation pay considered in *Lines*. Since they are not disposable by a wage earner until received, such refunds are distinguishable from other assets with a source in wages which have been allocated to a voluntary use by the wage earner." [Emphasis added.] Note, 87 Harv. L. Rev. 395, 403-04 (1973).

F. The Traditional Bankruptcy Principle That a Debtor Should Have a New Start Combines With the Equity Powers of the Court To Require That, on Balance, a Wage Earner's Involuntarily Withheld Income Tax Refund Is Exempt From the Claims of His Creditors.

Many of this Court's decisions in bankruptcy emphasize the "overriding consideration that equitable principles govern the exercise of bankruptcy jurisdiction". *Bank of Marin v. England*, 385 U.S. 99, 103 (1966). The fact that creditors in this case and the overwhelming majority of tax refund cases would receive only a pittance for their efforts has been fully documented. The balance, viewed in light of fairness, tips to the debtor who has deferred but necessary basic obligations which he counts on his tax refund to meet.

Even if the equities were equally compelling for each party, the traditional test of the "fresh start", free from pre-existing debt, must weight the scale to the wage earner. In *Perez v. Campbell*, 402 U.S. 637 (1971), the Court, speaking through Mr. Justice White, voided an

important and substantial creditor interest when it ruled that a state financial responsibility law, which "made 'it more probable that the debt will be paid despite the discharge' . . . frustrated Congress' policy of giving discharged debtors a new start". *Id.* at 650.

There is a guiding principle which emerges from the cases: If the possible asset is wages and is involuntarily withheld until a future date, since in the vast majority of cases the wages withheld will be used for future basic support or necessities of life, and will not provide any meaningful benefit to creditors, the asset should not be treated as "property" under Sec. 70a(5) of the Bankruptcy Act.

II.

EVEN IF THE REFUND IS PROPERTY VESTING IN THE TRUSTEE, 75% OF THE REFUND IS EXEMPT FROM GARNISHMENT BY THE TRUSTEE UNDER THE PROVISIONS OF THE CONSUMER CREDIT PROTECTION ACT.

The Consumer Credit Protection Act, 15 U.S.C. Sec. 1673, exempts from garnishment 75% of an individual's disposable earnings. The bankrupt argues here that the income tax refund, even if it is "property", is entitled to the 75% exemption enjoyed by all other wage payments under the provisions of the Consumer Credit Protection Act. Only if the income tax refund is "property" need the Court consider this question.

A. The Income Tax Refund Is Protected From Excessive Garnishment Because It Comes Within the Terms of the CCPA.

The trustee takes title to the bankrupt's property "except insofar as it is property which is held to be

exempt". Bankruptcy Act, Sec. 70(a), 11 U.S.C. Sec. 110a. The Bankruptcy Act does "not affect the allowance to bankrupts of the exemptions which are prescribed by the laws of the United States. . . ." Bankruptcy Act Sec. 6, 11 U.S.C. Sec. 24.

Such an exemption is that found in the Consumer Credit Protection Act, 15 U.S.C. Sec. 1671 *et seq.*, which exempts from garnishment 75% of an individual's disposable earnings. The trustee's claim to the income tax refund is a "garnishment" of "disposable earnings" within the statutory definitions.

Earnings

The basic statutory definition in the Consumer Credit Protection Act (CCPA) is that of "earnings". If the refund comes within that definition, it then falls into the protected category of disposable earnings.

" '[E]arnings' means compensation paid or payable for personal services, *whether denominated as wages*, salary, commission, bonus, *or otherwise*, and includes periodic payments pursuant to a pension or retirement program." 15 U.S.C. Sec. 1672(a). (Emphasis added.) There can be no dispute that the refund here consists entirely of compensation payable for personal services, even though it is "denominated as" an income tax refund.

On the face of the statute, then, the refund comes within the definition of earnings. As Judge Wollenberg noted:

> "There does not appear to be any reason of policy why the amount of the refund should be held to have lost its character as 'earnings' by reason of its somewhat circuitous route to the wage-earner's hands." *In re Cedor*, 337 F. Supp. 1103, 1107 (N.D. Cal. 1972); Accord, *In re Freedomland*, 480 F.2d 184, 190 (2d Cir. 1973).

Contrary to the assertion of the court below, the definition of earnings is not limited to weekly or periodic payments. The statutory definition itself contemplates such nonperiodic payments as a bonus or commission. It also contemplates earnings for pay periods other than weekly, when it mandates the Secretary of Labor to prescribe a formula for determining the exemption as to such pay periods. 15 U.S.C. Sec. 1673(a).

In accordance with the statute, the Secretary of Labor has promulgated a regulation which provides that, "The 25 percent part of the formula would apply to the *aggregate* disposable earnings for *all* the workweeks compensated". 29 C.F.R. Sec. 870.10(c)(1). [Emphasis added.] The tax refund may compensate for several workweeks, but under this regulation, the trustee could take only 25% of the aggregate.

It is irrelevant that the wages included in the refund may have been earned several weeks or months in the past. The statute makes no distinctions or exceptions that derive from the time of receipt. Moreover, the Secretary of Labor found inadequate a state statute which limited restrictions on garnishment to wages earned within the previous 30 days. He explained that "the garnishment restrictions of [the Act] apply without limitation as to when wages were earned". Op. WH-121 (Feb. 5, 1971). 6A BNA Labor Rel. Rep. WHM 95:198p, at q.

Disposable Earnings

To come within the protections of the CCPA, the refund must not only be "earnings", but "disposable earnings". The Consumer Credit Protection Act defines the term "disposable earnings" as "that part of the earnings of any individual remaining after the deduction from those earnings of any amounts required by law to be withheld". 15 U.S.C. Sec. 1672(b).

The refund is within the definition of "earnings". The entire amount is "disposable earnings" because nothing is required by law to be deducted or withheld from those earnings.[11] When the earnings comply with the definition of disposable earnings, that is, at the time the wages withheld for taxes are returned to the bankrupt, the restrictions on garnishment apply.

Garnishment

Garnishment is defined as "any legal or equitable procedure through which the earnings of any individual are required to be withheld for payment of any debt". 15 U.S.C. Sec. 1672(c).

In bankruptcy, the trustee is "vested by operation of law with the title of the bankrupt as of the date of the filing of the petition initiating a proceeding. . . ." Bankruptcy Act Sec. 70a, 11 U.S.C. Sec. 110a. He takes title to property as both an attaching and executing creditor. Bankruptcy Act. Sec. 70c, 11 U.S.C. Sec. 110c; Cowan, BANKRUPTCY LAW & PRAC., Sec. 623 (Supp. 1972).

"The process by which the trustee takes title is certainly 'a legal or equitable procedure', and the purpose of requiring the trustee to marshal the assets of the bankrupt is to pay the debts of the bankrupt." *In re Cedor*, 337 F. Supp. 1103 at 1107.

---

[11] "It is not material in determining whether sick pay constitutes earnings that it may not be subject to withholding and FICA deductions. Sick pay is included in the 'disposable earnings' to which the Act's garnishment restrictions apply because such pay is a component of compensation paid or payable for personal services or 'earnings'." Op. Secretary of Labor (Feb. 1, 1973), 6A BNA Labor Rel. Rep. WHM 95:198z, at aa.

Bankruptcy itself is a "legal or equitable procedure".[12] In addition, the referee here ordered Kokoszka to deliver the refund to the trustee. (App. 2). Such a court proceeding is one to which the Consumer Credit Protection Act applies. Op. Secretary of Labor WH-32 (May 18, 1970), 6A BNA Labor Rel. Rep. WHM 95:188.

Traditionally, garnishment refers to a levy upon a person who owes money to the debtor. But nothing in the Consumer Credit Protection Act definition of garnishment incorporates the traditional concept of a third party. Certainly the definition is not limited to situations where the employer possesses the funds.

> "Nor do we believe that the restrictions contained in section 303(a) of the Act are limited to situations where the exempt wages are still in the hands of the employer. . . . The restrictions apply to earnings *paid or payable. . . . Certainly we should not impose upon the statute restrictions or limitations which would tend to defeat or restrict the manifest purposes of the Act.*" [Emphasis added.] Op. Secretary of Labor WH-146 (Oct. 26, 1971) 6A BNA Labor Rel. Rep. WHM 95:198o, at p.

Recently, the Secretary of Labor sought and obtained an injunction against the practice of attaching or executing upon a paycheck as personal property. The Sheriff's argument was that attachment and execution are not garnishments under the CCPA. The court rejected this contention, saying:

---

[12] "[W]e regard an Internal Revenue Service attachment of wages for taxes due the United States as a 'legal procedure' within the meaning of Section 302(c) of Title III even in those cases where an actual court proceeding has not taken place." Op. Secretary of Labor WH-77 (Sept. 14, 1970), 6A BNA Labor Rel. Rep. WHM 95:197.

"[T]he Act applies to proceedings in aid of execution as well as attachment proceedings. This construction is clearly arrived at by an ordinary reading of the statutory language used in 15 U.S.C. Sec. 1672. The term "garnishment" is not restricted, but includes any procedure by which earnings of an individual are withheld. In view of this, whatever definition is given to "garnishment" for other purposes (those discussed in 30 AM JUR.2d *Executions* Sec. 1; 18 WORDS AND PHRASES 130, etc.), for the purpose of this decision the restrictions of the CCPA are applicable to proceedings under North Dakota law in aid of execution in all courts, as well as proceedings in 'execution of the judgment'." *Hodgson v. Christopher*, 365 F. Supp. 583, 586-87 (D. N.D. 1973).[13]

The refund ("earnings") is "required to be withheld" in several senses. First, title is required to be withheld when by operation of law, title to the refund vests in the trustee upon the filing in court of the bankruptcy petition.

Second, when the trustee notifies the Internal Revenue Service of his right to the refund, it is often sent by the IRS directly to the trustee in accordance with internal

[13]This interpretation is supported by the legislative history of the Consumer Credit Protection Act. As initially passed by the House, only 10% of the excess over $30 "of any wages, salary or earnings in the form of commission or bonus as compensation for personal services may be attached, garnished or subjected to any legal or equitable process or order". 114 Cong. Rec. (Feb. 1, 1968) H 713. In the conference committee, Congress increased the amount that could be garnished to 25% of the excess, but broadened the definition of earnings to cover all possible situations, and used a broad definition of the term garnishment to cover as many ways of taking as possible.

procedures. *In re Jones*, 337 F. Supp. 620, 621 (D. Minn. 1971). Indeed, the IRS views the refund as belonging to the trustee in bankruptcy. Rev. Rul. 72-387, 1972-2 C.B. 632. The refund is certainly withheld from the bankrupt in this event.

It is required to be withheld in a third sense when the bankruptcy court orders the bankrupt to turn over the refund or assist the trustee in obtaining it for the estate. (App. 2). If the bankrupt exercises any property rights in the refund thereafter, he risks denial of discharge or contempt proceedings. Bankruptcy Act Sections 14c(6), 41a(1); 11 U.S.C. Sections 32(c)(6), 69(a)(1).

Under the above analysis of the statutory terms, an income tax refund is within the restrictions against garnishment.

B. Other Provisions of the CCPA Confirm Its Applicability to the Income Tax Refund.

The application of the garnishment restrictions to the refund in a straight bankruptcy proceeding is mandated by the specific sections of the Consumer Credit Protection Act discussed above. It is also supported by other provisions of the CCPA.

The Congressional findings and declaration of purpose make it clear that the drafters of the garnishment sections were aware of the Bankruptcy Act as a whole and contemplated application of the garnishment sections to bankruptcy matters. In fact, the Consumer Credit Protection Act rests on both the bankruptcy and commerce powers of Congress. 15 U.S.C. Sec. 1671(b).

One of the concerns underlying the Consumer Credit Protection Act is the evil resulting from unrestricted garnishments. But a separate and distinct concern is that "the great disparities among the laws of the several states relating to garnishment have, in effect, destroyed the

uniformity of the bankruptcy laws and frustrated the purposes thereof in many areas of the country". 15 U.S.C. Sec. 1671(a)(3). On the basis of this finding, "Congress determines that the provisions of this subchapter [on garnishment restrictions] are necessary and proper . . . to establish uniform bankruptcy laws". 15 U.S.C. Sec. 1671(b).

As noted *supra* p. 20, the bankruptcy laws are anything but uniform with respect to treatment of income tax refunds. A decision that only 25% of any such refund passes to the trustee would establish a more nearly uniform rule and insure that debtors are treated comparably regardless of their residence. It would also further the intent of Congress.

Further, the Consumer Credit Protection Act provides that the garnishment restrictions do not apply to "any order of any court of bankruptcy under Chapter XIII of the Bankruptcy Act". 15 U.S.C. Sec. 1673(b)(2).[14] "[U]nless the Sec. 1673(b)(2) exception of orders in Chapter XIII proceedings is surplusage, Congress must have intended that the Act's restrictions on garnishment should apply to other, similar orders of the bankruptcy court not within the terms of the exception," *In re Cedor*, 337 F. Supp. 1103, 1107 (N.D. Cal. 1972).

For instance, orders under Sec. 17c(3), 11 U.S.C. Sec. 35c(3) ("render judgment and make all orders necessary for the enforcement thereof") would be subject to the 25% garnishment limitation in accordance with the intent

---

[14]Chapter XIII gives the bankruptcy court the power to order the employer of a Chapter XIII debtor to withhold from the bankrupt's pay and turn over to the trustee whatever periodic amounts the debtor has agreed to pay to the trustee under the terms of his wage earner plan.

of the statute. And, where the trustee takes title to wages for services already performed, "The limitations of the Consumer Credit Protection Act will cut down the right of the trustee to 25% of the wages. . . ." Cowan, BANKRUPTCY LAW & PRAC. Sec. 623 (Supp. 1972).

After establishing restrictions on garnishment, and three narrow exceptions thereto, Congress underscores its intent. "No court of the United States or any State may make, execute, or enforce any order or process in violation of this section." 15 U.S.C. Sec. 1673(c).

Congress acted in contemplation of the Bankruptcy Act with the intent to promote uniform bankruptcy laws. It adopted definitions which include the income tax refund. In any event, the statute, being a remedial one, must be broadly construed to effectuate its purpose. *Wilder v. Inter-Island Steam Nav. Co.*, 211 U.S. 239, 246 (1908) (statute protecting seamen's wages liberally interpreted); *Peyton v. Rowe*, 391 U.S. 54, 65 (1968); *Tcherepnin v. Knight*, 389 U.S. 332, 336 (1967).

C. The Interpretations of the Secretary of Labor Support Bankrupt's Position.

The Secretary of Labor, acting through the Wage and Hour Division, is charged with the enforcement of the garnishment provisions of the Consumer Credit Protection Act. 15 U.S.C. Sec. 1676. This Court has frequently applied the "venerable principle that the construction of a statute by those charged with its execution should be followed unless there are compelling indications that it is wrong. . . ." *Red Lion Broadcasting Co. v. FCC*, 395 U.S. 367, 381 (1969); *Lewis v. Martin*, 397 U.S. 552, 559 (1970); *Zemel v. Rusk*, 381 U.S. 1, 11 (1965).

Interspersed in the above arguments were certain of the agency's interpretations which support bankrupt's

position. More to the point, an opinion of Robert D. Moran, Wage and Hour Administrator, states in full:

> "This is in reply to your letter of October 21, 1970, concerning Title III, Restriction on Garnishment, of the Consumer Credit Protection Act.
>
> It is not clear from your letter whether a voluntary petition in bankruptcy is involved or whether there has been a petition filed under Chapter XIII of the Bankruptcy Act. The exemption in section 303(b)(2) of the Act runs only to orders of the Bankruptcy Court under Chapter XIII. *Any other order* of a Bankruptcy Court would appear subject to the garnishment restrictions provided in Section 303(a)." [Emphasis added.] Op. WH-103, Dec. 18, 1970, 6A BNA Labor Relations Rep. WHM 95:198h.

Thus, the Wage and Hour Division interprets the garnishment restrictions literally to accomplish the purpose of the statute to protect the wage earner. It has stated that "[T]he garnishment restrictions of Title III apply without limitation as to when wages were earned". And, "Under Title III, a garnishment writ may *never* cause *any* withholding of *any* earnings in excess of that subjected to garnishment under section 303(a)". [Emphasis added.] Op. Secretary of Labor WH-121 (Feb. 5, 1971), 6A BNA Labor Rel. Rep. WHM 95:198p.

Under the interpretations of the Wage and Hour Division, the earnings of a debtor do not lose their exempt character by being deposited by the employer in a bank account:[15]

---

[15] "[I]t is believed that employees generally withdraw all of the funds before the next pay day." Op. Secretary of Labor WH-146 (Oct. 26, 1971), 6A BNA Labor Rel. Rep. WHM 95:198o.

"The Act's restrictions apply to earnings or compensation paid or payable for personal services. It would be contrary to the express mandate of the Act to assume that when a debtor deposits his earnings for safekeeping in a bank, his earnings are transformed into a bank credit to which the Act's restrictions do not apply." Op. Secretary of Labor WH-171, (Aug. 3, 1972) 6A BNA Labor Rel. Rep. WHM 95:198r.

A fortiori, when wages are "deposited" with the United States Government by the employer, and the debtor cannot choose to expend or invest them, they are capable of identification as earnings and subject to the restrictions on garnishment.

Thus, the interpretations of the administering agency support bankrupt's position that his refund remains earnings and 75% of the refund is protected from garnishment by the trustee.

CONCLUSION

The bankrupt here seeks a ruling that his income tax refund is not property of his estate in bankruptcy. Such a ruling would implement the basic purpose of the Bankruptcy Act to give him a fresh start in life. A contrary ruling would provide only a token benefit to creditors.

---

[15] *(cont.)*

Op. WH-171, quoted in the text, cites a number of cases in which payments, such as veteran's benefits or workmen's compensation, retain their exempt character when deposited by the debtor in a bank account, when such payments are necessary or intended for the support of the debtor. In *Lawrence v. Shaw*, 300 U.S. 245 (1937), this Court stated that such exempt payments retain their exemption "until expended or invested" under the statute there interpreted.

Alternatively, the bankrupt contends that the trustee is entitled to no more than 25% of the wages returned to him in the form of an income tax refund, under the Consumer Credit Protection Act. Such a ruling would accomplish Congress' intent to protect a wage earner's income, whatever form it takes.

For all of the reasons above stated, this Court is respectfully requested to reverse the ruling of the Second Circuit Court of Appeals.

JOANNE S. FAULKNER
New Haven Legal Assistance
Association, Inc.
169 Church Street
New Haven, Connecticut 06510
(203) 772-3340

Counsel for Petitioner

JOSEPH DEAN GARRISON, JR.
FREDERICK W. DANFORTH, JR.
New Haven Legal Assistance
Association, Inc.

THOMAS R. ADAMS
Legal Aid Society of
San Mateo County
7324 Mission Street
Daly City, California 94104
(415) 755-8550

JOHN T. HANSEN
MICHAEL H. WEISS
Hansen, Jaffe & Weiss
555 Polk Street, Suite 201
San Francisco, California 94102
(415) 771-5281

Appendix A

The statutory provisions involved herein are as follows: Bankruptcy Act §6 (11 U.S.C. §24), which states:

> "This title shall not affect the allowance to bankrupts of the exemptions which are prescribed by the laws of the United States or by the State laws in force at the time of the filing of the petition in the State wherein they have had their domicile for the six months immediately preceding the filing of the petition, or for a longer portion of such six months than in any other State: *Provided, however,* That no such allowance shall be made out of the property which a bankrupt transferred or concealed and which is recovered or the transfer of which is avoided under this title for the benefit of the estate, except that, where the voided transfer was made by way of security only and the property recovered is in excess of the amount secured thereby, such allowance may be made out of such excess."

Bankruptcy Act §70a (11 U.S.C. §110a), which states:

> "(a) The trustee of the estate of a bankrupt and his successor or successors, if any, upon his or their appointment and qualification, shall in turn be vested by operation of law with the title of the bankrupt as of the date of the filing of the petition initiating a proceeding under this title, except insofar as it is to property which is held to be exempt, to all of the following kinds of property wherever located (1) documents relating to his property; (2) interests in patents, patent rights, copyrights, and trade-marks, and in ap-

plications therefor: *Provided,* That in case the trustee, within thirty days after appointment and qualification, does not notify the applicant for a patent, copyright, or trade-mark of his election to prosecute the application to allowance or rejection, the bankrupt may apply to the court for an order revesting him with the title thereto, which petition shall be granted unless for cause shown by the trustee the court grants further time to the trustee for making such election; and such applicant may, in any event, at any time petition the court to be revested with such title in case the trustee shall fail to prosecute such application with reasonable diligence; and the court, upon revesting the bankrupt with such title, shall direct the trustee to execute proper instruments of transfer to make the same effective in law and upon the records; (3) powers which he might have exercised for his own benefit, but not those which he might have exercised solely for some other person; (4) property transferred by him in fraud of his creditors; (5) property, including rights of action, which prior to the filing of the petition he could by any means have transferred or which might have been levied upon and sold under judicial process against him, or otherwise seized, impounded, or sequestered: *Provided,* That rights of action ex delicto for libel, slander, injuries to the person of the bankrupt or of a relative, whether or not resulting in death, seduction, and criminal conversation shall not vest in the trustee unless by the law of the State such rights of action are subject to attachment, execution, garnishment, sequestration, or other judicial process: *And provided further,* That when any bankrupt, who is a natural person, shall

have any insurance policy which has a cash surrender value payable to himself, his estate, or personal representatives, he may, within thirty days after the cash surrender value has been ascertained and stated to the trustee by the company issuing the same, pay or secure to the trustee the sum so ascertained and stated, and continue to hold, own, and carry such policy free from the claims of the creditors participating in the distribution of his estate under the bankruptcy proceedings, otherwise the policy shall pass to the trustee as assets; (6) rights of action arising upon contracts, or usury, or the unlawful taking or detention of or injury to his property; (7) contingent remainders, executory devises and limitations, rights of entry for condition broken, rights or possibilities of reverter, and like interests in real property, which were nonassignable prior to bankruptcy and which, within six months thereafter, become assignable interests or estates or give rise to powers in the bankrupt to acquire assignable interests or estates; and (8) property held by an assignee for the benefit of creditors appointed under an assignment which constituted an act of bankruptcy, which property shall, for the purposes of this title, be deemed to be held by the assignee as the agent of the bankrupt and shall be subject to the summary jurisdiction of the court.

All property, wherever located, except insofar as it is property which is held to be exempt, which vests in the bankrupt within six months after bankruptcy by bequest, devise or inheritance shall vest in the trustee and his successor or successors, if any, upon his or their appointment and qualification, as of the date when it vested in

the bankrupt, and shall be free and discharged from any transfer made or suffered by the bankrupt after bankruptcy.

All property, wherever located, except insofar as it is property which is held to be exempt, in which the bankrupt has at the date of bankruptcy an estate or interest by the entirety and which within six months after bankruptcy becomes transferable in whole or in part solely by the bankrupt shall, to the extent it becomes so transferable, vest in the trustee and his successor or successors, if any, upon his or their appointment and qualification, as of the date of bankruptcy.

The title of the trustee shall not be affected by the prior possession of a receiver or other officer of any court."

Consumer Credit Protection Act, 15 U.S.C. §1671, entitled "Congressional Findings and Declaration of Purpose", states:

(a) The Congress finds:

(1) The unrestricted garnishment of compensation due for personal services encourages the making of predatory extensions of credit. Such extensions of credit divert money into excessive credit payments and thereby hinder the production and flow of goods in interstate commerce.

(2) The application of garnishment as a creditors' remedy frequently results in loss of employment by the debtor, and the resulting disruption of employment, production, and consumption constitutes a substantial burden on interstate commerce.

(3) The great disparities among the laws of several States relating to garnishment have, in effect, destroyed the uniformity of the bankruptcy laws and frustrated the purposes thereof in many areas of the country.

(b) On the basis of the findings stated in subsection (a) of this section, the Congress determines that the provisions of this subchapter are necessary and proper for the purpose of carrying into execution the powers of the Congress to regulate commerce and to establish uniform bankruptcy laws."

C.C.P.A., 15 U.S.C. §1672, entitled, "Definitions", states:

"For the purpose of this subchapter:

(a) The term 'earnings' means compensation paid or payable for personal services, whether denominated as wages, salary, commission, bonus, or otherwise, and includes periodic payments pursuant to a pension or retirement program.

(b) The term 'disposable earnings' means that part of the earnings of any individual remaining after the deduction from those earnings of any amounts required by law to be withheld.

(c) The term 'garnishment' means any legal or equitable procedure through which the earnings of any individual are required to be withheld for payment of any debt."

C.C.P.A., 15 U.S.C. §1673, entitled, "Restrictions on Garnishment—Maximum Allowable Garnishment", states:

"(a) Except as provided in subsection (b) of this section and in section 1675 of this title, the

maximum part of the aggregate disposable earnings of an individual for any workweek which is subjected to garnishment may not exceed

(1) 25 per centum of his disposable earnings for that week, or

(2) the amount by which his disposable earnings for that week exceed thirty times the Federal minimum hourly wage prescribed by Section 206(a) (1) of Title 29 in effect at the time the earnings are payable.

whichever is less. In the case of earnings for any pay period other than a week, the Secretary of Labor shall by regulation prescribe a multiple of the Federal minimum hourly wage equivalent to that set forth in paragraph (2).

Exceptions

(b) The restrictions of subsection (a) of this section do not apply in the case of

(1) any order of any court for the support of any person.

(2) any order of any court of bankruptcy under chapter XIII of the Bankruptcy Act.

(3) any debt due for any State or Federal tax.

Execution or enforcement of garnishment order or process prohibited

(c) No court of the United States or any State may make, execute, or enforce any order or process in violation of this section."

IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1973

No. 73-5265

HENRY A. KOKOSZKA, Bankrupt,

Petitioner,

v.

RICHARD BELFORD, Trustee in Bankruptcy of the Estate of Henry A. Kokoszka, Bankrupt,

Respondent.

ON WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

BRIEF OF AMICUS CURIAE IN SUPPORT OF THE JUDGMENT BELOW

Of Counsel:

JAMES L. LEKIN
HARRY D. SHAPIRO
Venable, Baetjer and Howard

BENJAMIN R. CIVILETTI
VENABLE, BAETJER AND HOWARD
2 Hopkins Plaza
Baltimore, Maryland 21201

Amicus Curiae

Washington, D.C. • CLB PUBLISHERS' • LAW PRINTING CO. • (202) 393-0625

TABLE OF CONTENTS

TABLE OF AUTHORITIES

IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1973

No. 73-5265

HENRY A. KOKOSZKA, Bankrupt,

Petitioner,

v.

RICHARD BELFORD, Trustee in Bankruptcy of the Estate of Henry A. Kokoszka, Bankrupt,

Respondent.

ON WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

BRIEF OF AMICUS CURIAE IN SUPPORT OF THE JUDGMENT BELOW

INTEREST OF AMICUS CURIAE

This brief is submitted pursuant to the Court's invitation of March 4, 1974 to the undersigned to brief and argue this case as *Amicus Curiae* in support of the judgment below.

PRELIMINARY STATEMENT

Respondent adopts the material in Petitioner's brief under the headings "OPINIONS BELOW", "JURISDICTION", "STATUTES INVOLVED" and "STATEMENT OF THE CASE".

QUESTIONS PRESENTED

1. Is an income tax refund due Petitioner-bankrupt "property" which passes to the trustee under Section 70a(5) of the Bankruptcy Act?

2. If the income tax refund is "property" within the meaning of Section 70a(5) of the Bankruptcy Act, do the garnishment provisions of the Consumer Credit Protection Act preclude the bankruptcy trustee from taking the entire refund?

SUMMARY OF ARGUMENT

I. and II. Legislative history and relevant decisions of this Court support a broad interpretation of what is "property" within the meaning and scope of Section 70a(5) of the Bankruptcy Act. The Bankruptcy Act permits the bankrupt to withhold from his creditors those assets which are exempt under (1) the laws of the state where he resides and (2) statutes of the United States. The State of Connecticut does not exempt an income tax refund from the claims of creditors. Likewise, there is no Federal statue providing for such an exemption.

The "fresh start" doctrine embodies the benefits flowing to the debtor from bankruptcy – relief from

the obligation of pre-bankruptcy debts, retention of exempt property provided in Section 6 of the Act, and freedom to accumulate future wealth. None of the relevant cases decide, or even suggest, that a "fresh start" permits a bankrupt to withhold from the trustee what would otherwise be "property" unless the asset is exempt or some right is provided in Section 70a – the bankrupt can acquire his life insurance policy from the trustee by paying the cash surrender value. Moreover, *Legg v. St. John*, 296 U.S. 489 (1936), holds that the "fresh start" doctrine is inapplicable to a situation in principle the same as the one presented before this Court.

An income tax refund which was due as of the date of bankruptcy is "property" within the meaning of Section 70a(5) of the Bankruptcy Act. *Segal v. Rochelle*, 382 U.S. 375 (1965), involved a similar issue and this Court determined that income tax refunds relating to taxable events occurring before bankruptcy were "sufficiently rooted in pre-bankruptcy past and so little entangled with the bankrupts' ability to make an unencumbered fresh start that it should be regarded as "property" under §70a(5)". The decision in *Lines v. Frederick*, 400 U.S. 18 (1970), is inapplicable and distinguishable because vacation and layoff pay accrued but unpaid at the time of bankruptcy, was determined by this Court to be "future wages". One of the bankrupts could collect the sum either during the annual period when his employer shut down the plant, or on termination of his employment. The other bankrupt could draw it either on termination or under a conventional voluntary vacation plan. According to this Court, without the layoff or vacation pay, the bankrupts would not achieve the "new opportunity in

life and [the] clear field for future effort, unhampered by the pressure and discouragement of pre-existing debt".

III. Petitioner requests this Court to amend judicially the present Bankruptcy Act by (1) determining that an income tax refund is not "property" within the meaning of Section 70a(5) or (2) ruling that an income tax refund is "exempt", contrary to Section 6 of the Bankruptcy Act and the laws of the State of Connecticut. Furthermore, the proposed Bankruptcy Act of the Commission on the Bankruptcy Laws of the United States, pending in the Congress, offers a more preferable and traditional method of amending the Bankruptcy Act.

IV. The Consumer Credit Protection Act ("CCPA") does not preclude the trustee from taking the entire refund within the bankruptcy estate. The legislative history of the CCPA clearly indicates an intent to correct problems and abuses through garnishment of an employee's wages outside a bankruptcy proceeding. An income tax refund is not "earnings" or "disposable earnings" within the definitions of Section 1672(a) and (b) of the CCPA. Moreover, the trustee's taking of the refund is not "garnishment" within the definition of Section 1672(c) of the CCPA.

ARGUMENT

I.

THE LEGISLATIVE HISTORY OF SECTION 70a(5) OF THE BANKRUPTCY ACT MANIFESTS AN INTENT BY CONGRESS TO GIVE THE TERM "PROPERTY" A BROAD DEFINITION AND CONGRESS INTENDED TO PROTECT THE INTERESTS OF THE BANKRUPT THROUGH SECTION 6 OF THE BANKRUPTCY ACT.

A. Legislative Background of Section 70a(5) of the Bankruptcy Act.

In order to gain a proper perspective of the meaning of "property" as the word is used in Section 70a of the Bankruptcy Act, one must journey through the history of bankruptcy legislation in the United States. The Bankruptcy Act of 1800 represented the nation's first Federal bankruptcy legislation.[1] Among other provisions, the Act provided that upon a declaration that the debtor was bankrupt, duly appointed commissioners of the bankrupt were empowered to take into their possession "all the estate, real and personal, of every nature and description to which the said bankrupt may be entitled, either in law or equity, in any manner whatsoever", excluding certain specified Federal exemptions of "necessary wearing apparel" and "necessary beds and bedding".[2] The estate of the bankrupt also included all debts due to such bankrupt or to any other person for the bankrupt's use or benefit.[3] If any estate,

---

[1] 4A Collier, Bankruptcy, P. 23, §70.02[2](14th Ed. 1971) (hereinafter called "Collier").

[2] Act of April 4, 1800, §5, 2 Stat. 19. Each of the United States Bankruptcy Acts is set forth in 10 Collier, Appendix.

[3] *Id.* §13.

real or personal, descended, reverted to, or became vested in any person after being declared a bankrupt and prior to that person obtaining a certificate of discharge, such estate vested in the commissioners.[4] This Act was repealed in 1803.

The next Federal bankruptcy statute was the Bankruptcy Act of 1841.[5] Like its predecessor, the Act of 1841 broadly described the assets of the bankrupt which vested in the trustee (termed the "assignee") as "all the property and rights of property, of every name and nature, and whether real, personal, or mixed".[6] Specified household articles and wearing apparel were exempted, along with other articles not to exceed the sum of $300.00 in the discretion of the assignee.[7] There was no definition of the term "property". This Act also was shortlived and was repealed in 1843. The next bankruptcy act – the Act of 1867 – likewise failed to define "property" but described the "property" and "estate" of the bankrupt in similarly broad terms.[8] The Act of 1867 was repealed in 1878.

In 1898, the present Section 70a was enacted. Entitled "title to Property", Section 70a, as enacted,[9] provided generally that the trustee of the estate of a bankrupt was vested by operation of law with the title of the bankrupt, as of the date he was adjudged a

---

[4] *Id.* §50.

[5] Act of August 19, 1841, 5 Stat. 440.

[6] *Id.* §3.

[7] *Id.*

[8] Act of March 2, 1867, §15, C. 176, 14 Stat. 517.

[9] Act of July 1, 1898, §70a, C. 541, 30 Stat. 544, *as amended,* 11 U.S.C. §110.

bankrupt, to all assets and property as specified thereafter. The relevant portion of the provision, subsection (5), described the bankrupt's estate as all "property which prior to the filing of the petition [the bankrupt] could by any means have transferred or which might have been levied upon and sold under judicial process against him."[10] Again, there was no definition of the term "property".

Section 70 was substantially amended by the Act of 1938, popularly known as the Chandler Act.[11] Specifically the wording of Section 70a was modified to provide that the trustee of the estate was vested by operation of law with the title of the bankrupt as of the date of the filing of the petition in bankruptcy.[12] Under subsection (5) of Section 70a, the trustee was vested with all "property, *including rights of action*, which prior to the filing of the petition [the bankrupt] could by any means have transferred or which might have been levied upon and sold under judicial process against him." (emphasis added)[13] There were other changes relating to: (1) property rights which vested within six months after bankruptcy through bequest, devise, or inheritance, and (ii) property in which the bankrupt had on the date of bankruptcy an estate or an interest by the entirety.[14]

---

[10] *Id.*, subsection 5.

[11] Act of June 22, 1938, C. 575, 52 Stat. 879, *amending*, 11 U.S.C. §1 *et seq.*

[12] *Id.* §1; The Act of 1898 provided that the property vested "as of the date [the bankrupt] was adjudged a bankrupt".

[13] *Id.*

[14] *Id.*

Section 70a was further amended in 1952 to vest in the trustee by operation of law all property of the bankrupt wherever located.[15] Otherwise, Section 70a has remained unchanged since the Chandler Act became law.

The history of bankruptcy legislation indicates that Congress never attempted to define specifically the word "property" in the context of bankruptcy legislation. Past bankruptcy legislation does reveal, however, that Congress intended the word to have a very broad defintion, so as to effect a transfer of all of the bankrupt's assets, whether in the form of tangible goods or rights, to the trustee for distribution to creditors.[16] In fact, "property" first appeared in the 1841 Act as part of a phrase "property of every name and nature".[17] Section 70a of the present Act provides creditors with their primary remedy under the Act and, in that sense, the Section can be said to be creditor oriented.[18] Had Congress intended to withhold certain

---

[15]Act of July 7, 1952, §23, C. 579, 66 Stat. 429, *amending*, 11 U.S.C. §1 *et seq.*

[16]For general background and the legislative history of bankruptcy laws in the United States, see 1 *Collier*, Pars. 0.01 through 0.08 and Charles Warren, *Bankruptcy in United States History*, Harvard University Press, 1935; see also Comment, *Aspects of the Chandler Bill to Amend the Bankruptcy Act*, 4 University of Chicago L.R. 369 (1936-37); Comment, *Bankruptcy Exemptions: Critique and Suggestions*, 68 Yale L.J. 1459 (1959); and Comment, *Bankruptcy Exemptions: A Full Circle Back to the Act of 1800?* 53 Cornell L.R. 663 (1968).

[17]Note 5, *supra.*

[18]In this sense, Section 70 can be contrasted with the "exemption" (Section 6) and "discharge" (Section 14) sections of the Act which provide protection to the bankrupt.

property interests from creditors –as it did by creating exemptions – one would imagine that these interests would be specifically enumerated.

Other forms of legislative history are less helpful in ascertaining the scope of Section 70a. Specifically, Congress made no effort in legislative reports or debates to detail the types of interests or rights which should be included within the term "property". Congressional debate on the present Bankruptcy Act, however, at least indicates a Congressional intent to preserve in that Act the inclusive definition given to "property" in earlier acts. Senate Bill 1035,[19] which became the Bankruptcy Act of 1898, was reported from Committee in the House of Representatives by Representative Henderson of Iowa, Chairman of the Committee on the Judiciary. In explaining Section 70 under the general heading, "The Estate", Representative Henderson noted that "property *of every kind and description* which prior to the filing of the petition might by any means have been transferred by the bankrupt or which might have been levied upon and sold under judicial process against him, will vest in the trustee". (emphasis added)[20]

In conclusion, the legislative history of bankruptcy statutes from the Bankruptcy Act of 1800 to the most recent amendments of the present Act does not address the precise question of whether a tax refund due a bankrupt is "property" within the meaning of §70a(5). The Federal income tax laws did not provide for

---

[19]55 Cong., 2d Sess. (1897).

[20]31 Cong. Rec. 1788 (1898) (Remarks of Representative Henderson).

withholding of income taxes until 1943,[21] and since 1943, as indicated above, there has been virtually no legislation dealing with Section 70a. One thing is clear, however. The word – "property" – within the context of Section 70a and preceding bankruptcy acts has been given as broad a meaning as possible.

B. Legislative Background of Section 6 of the Bankruptcy Act.

Congress' intent to give the term "property" a very broad construction becomes more apparent when Section 70a is read in conjunction with Section 6 of the Bankruptcy Act, – entitled "Exemptions of Bankrupts".[22] Section 70a is essentially a creditor-oriented provision securing to the creditors the property of the bankrupt. The bankrupt's interests are then brought to bear through Section 6.

The purpose of Section 6 is to exempt certain property of the bankrupt from seizure by his creditors, giving him the property exemptions in force in his domiciliary state, together with any applicable Federal exemptions. The protective effect of Section 6 is reflected in Section 70a of the Act, which excludes exempt property from the bankrupt's estate.

The history of the Bankruptcy Act and its predecessor acts make clear that Congress included Section 6 in the Act to assure that bankrupts would have an opportunity to make a "fresh start",

---

[21]Current Tax Payment Act of 1943, 1943 Cum. Bull. 1239; H. Rept. No. 401, 78 Cong., 1st Sess., 1943 Cum. Bull. 1283; S. Rept. No. 221, 78th Cong., 1st Sess., 1943 Cum. Bull. 1314.

[22]11 U.S.C. §24.

unencumbered by their prior debts. Congress decided that this purpose could best be achieved through incorporation of the individual exemption laws of the various states.

This purpose of Section 6 becomes obvious when the Section is read in historical context. Each of the United States bankruptcy statutes, beginning with the Bankruptcy Act of 1800, made some provision for protecting certain items of property from seizure by creditors.

As previously noted, the Act of 1800, and the subsequent Bankruptcy Act of 1841, dealt with exemptions by specifying items of property which could be retained by the bankrupt. No reference was made to state law. Both of these acts, however, had very short duration[23] and during the interim periods when no Federal bankruptcy statutes were in effect, the individual states adopted their own insolvency laws to deal with creditor-debtor problems.[24] These statutes generally listed homestead and other real and personal property which were exempt from seizure by creditors. These listings varied widely from state to state.[25]

In the 1860's, following the financial panic of 1857, pressure again mounted for a Federal bankruptcy statute. In order to gain support from western states, which generally had adopted broad exemptions in their insolvency laws, Congress incorporated state exemptions within the context of a Federal bankruptcy statute –

---

[23]As previously noted, the Bankruptcy Act of 1800 was repealed in 1803 and the Bankruptcy Act of 1841 was repealed in 1843.

[24]Warren, *supra*, noted 16, at 91.

[25]*Id.* at 100.

which became the Bankruptcy Act of 1867.[26] This same concept was repeated when Section 6 was adopted in the present Bankruptcy Act of 1898.

A great deal of Congressional concern was expressed in 1867 and 1898 that the Acts, by incorporating state exemptions, would not meet the constitutional requirements of uniformity.[27] This concern was apparent in the speech of Representative Henderson, Chairman of the Committee on the Judiciary, when he opened the debate on S.B. 1035[28] which was enacted to become the Bankruptcy Act of 1898, as follows:

> "The exemptions of the bankrupt will be allowed as prescribed by the State laws in force at the time of the filing of the petition in the State wherein he had his domicile for six months, or the greater portion thereof, immediately preceding the filing of the petition.
>
> "It has been suggested that since the exemption as provided by each of the States is different from those provided by every other State, a law which does not interfere with them may be unconstitutional because not uniform. There are two replies to his suggestion: The first is that the last bankruptcy law recognized the validity of the exemption of the State laws as of a certain date and notwithstanding such provision was held to be constitutional by the courts.
>
> "The second reply is, that the proposed law does not undertake to confirm, or to in any sense

---

[26]The Bankruptcy Act of 1867 was repealed in 1878.

[27]The Supreme Court upheld the constitutionality of Section 6 in *Hanover National Bank v. Moyses*, 186 U.S. 181 (1901).

[28]Note 19, *supra*.

enact, the laws as in force in the several States, but simply refuses to interfere with such laws or to make any provision for providing other exemptions for bankrupts. If the law should be criticised in this, that it does not provide a uniform exemption different from the States or undertake to exercise any control over State legislation upon that subject, the reply is that it is not necessary for it to do so as a legal proposition, and that it is impracticable for it to do so as a matter of policy.

"The needs of the poor man in each of the States is different from the needs of poor men similarly situated in other States – that is to say, in order for an insolvent debtor to protect his family from want in, say Florida, he must have household belongings of quite a different character than would be necessary if he was a resident of, say, Maine or Oregon. If it would undertake to provide a uniform exemption in money value, the same difficulties would be encountered.

"That is to say, the amount that would be necessary to provide the modest belongings which the insolvent debtor should have for the needed protection of his family in, say, Connecticut, would be very much less than would be required for the same debtor to make like provision if he were a citizen of Montana or Texas.

"In view of all which it has been thought advisable by the committee not to endeavor to utilize the bankruptcy law as a means of correcting State legislation on this important subject. Those who may fear that the bill on this account is

unconstitutional may calm their fears, as there is not the slightest danger in this respect."[29]

The above remarks, appear from seeking to appease those members of Congress who felt this section was unconstitutional, give broad insight into Congress' view of the purpose of Section 6. Most importantly, Representative Henderson's remarks establish that Congress intended that the state exemptions authorized in Section 6 be the only exemptions available to bankrupts under the Act, i.e., Congress "refuses . . . to make any provision for providing other exemptions for bankrupts". Congress, for policy reasons, left to the individual states the task of determining how much and what type of property should be retained by the bankrupt, and thereby reconciled the debtor and creditor interests inherent in this decision.

The Chandler Act of 1938[30], which materially amended the Act of 1898, made no basic change in Section 6. An amendment was adopted which added to Section 6 any exemption "prescribed by the laws of the United States". This amendment carried over to the Act the exemptions for pensions, soldiers' bonuses, and other payments which were then contained in other Federal statutes.[31] Provisions were also added to Section 6 which (1) provided that no exemption should be taken out of fraudulently transferred property

---

[29]31 Cong. Rec. 1787 (1898) (Remarks of Representative Henderson).

[30]Note 11, *supra.*

[31]Remarks of Mr. Adair, Member, National Bankruptcy Committee, Hearings on H.R. 6439, *Revision of the Bankruptcy Act,* before the House Committee, June 1-9, 1937.

recovered by the estate and (2) clarified the definition of domicile for the bankrupt. No other Federal exemption, general or otherwise, was added to the Act.

The 1938 Chandler Act was written by a group known as the National Bankruptcy Conference in conjunction with the House Committee on the Judiciary.[32] The following remarks of one of the Conference members, Mr. Jacob I. Weinstein, during the 1937 hearings on the legislation, are interesting insofar as they express why the Conference decided not to adopt national exemptions in place of the state exemptions embodied in Section 6:

> "The National Conference has given this subject careful study. At one of its early sessions it considered the advisability, for the purposes of the Bankruptcy Act, either establishing an absolute uniformity of exemptions in disregarding the varying State laws or of permitting the present diversity of exemptions to remain, but with a limitation upon the maximum amount of such exemptions. It found, however, that the subject necessarily involved a study of the exemption statutes of each State and of the State decisions thereunder, and of the local conditions and circumstances which give rise to these varying exemption allowances. After a cursory examination of the various exemption laws it being apparent to us that in the present economic condition of the country, it would be most inadvisable to attempt any changes. It also occurred to us that any limitation on the present exemption allowed under the bankruptcy law would be met with vigorous political opposition, particularly from the repre-

[32]H. Rept. No. 1409, 75th Cong., 1st Sess., 2-3 (1937).

sentatives of farmer States. Therefore, we abandoned for the present the drafting of a uniform exemption provision."[33]

In conclusion, the Congressional intent first expressed by Congress in 1898 when it enacted Section 6 is still embodied in that Section today. State exemptions[34] are the exclusive means by which Congress intended to protect the property of bankrupts from seizure by creditors.

In prior decisions, this Court has itself recognized that Congress decided to rely on state exemption laws rather than establishing general Federal exemptions. In *Holden v. Stratton*, 198 U.S. 202 (1905), the Court had occasion to reconcile the exemption provisions of Section 6 with the provisions of Section 70a(5) which specifically dealt with the disposition of life insurance policies. The question in that case was whether a life insurance policy, admittedly exempt under Washington state law, passed to the bankrupt by virtue of the state exemption or to the trustee by virtue of the specific proviso in Section 70a(5) dealing with life insurance. The Court held that Section 6 qualified the entire Section 70a, including the portion dealing with life insurance, and the policy passed to the bankrupt. In so holding, the Court noted that "[i]t has always been the policy of Congress, both in general legislation and in

---

[33]Hearing on H.R. 6439, note 31, *supra* at 388. Mr. Weinstein introduced with his remarks a table comparing the various state property exemptions then in force.

[34]As noted, the Chandler Act of 1938 added to Section 6 any exemption "prescribed by the laws of the United States". See note 31, *supra*.

bankrupt acts, to recognize and give effect to the state exemption laws". 198 U.S. at 213-214.

The Court's recognition of state exemptions as the exclusive means by which bankrupts were allowed to retain some property was set forth in *Hanover National Bank v. Moyses*, 186 U.S. 181 (1901). In that case, the Court was faced with the contention that Section 6, by incorporating various state exemptions into the Act, rendered the 1898 Act unconstitutional as not being "uniform" under the Constitution. The Court rejected this argument stating that the Act was uniform "when the trustee takes in each state whatever would have been available to the creditors if the bankrupt law had not been passed". 186 U.S. at 190. This quote implicitly recognized the absence of any general Federal exemptions under the Act.

In sum, Congress' decision to adopt state exemptions within the context of the Bankruptcy Act represents an obvious compromise between debtor and creditor interests. On the one hand, such exemptions represent Congressional intent to preserve certain items of property for the bankrupt. On the other hand, the very existence of exemptions reaffirms the concept that all property *not* exempt is to be vested in the trustee for distribution to creditors.

II.

A TAX REFUND IS "PROPERTY" WITHIN THE MEANING OF SECTION 70a(5) OF THE BANKRUPTCY ACT

A. The development of the "fresh start" doctrine prior to *Segal v. Rochelle* and *Lines v. Frederick*.

In *Wetmore v. Markoe*, 196 U.S. 68 (1904), this Court held that alimony arrears awarded to a wife

against her former husband for support of herself and their children in accordance with a final decree of absolute divorce was not a provable debt barred by discharge in bankruptcy. After a discussion of the merits of the case, the Court made the following observation (at 77):

> "... Systems of bankruptcy are designed to relieve the honest debtor from the weight of indebtedness which has become oppressive and to permit him to have a *fresh start* in business or commercial life, freed from the obligation and responsibilities which may have resulted from business misfortunes. Unless positively required by direct enactment the courts should not presume a design upon the part of Congress in relieving the unfortunate debtor to make the law a means of avoiding enforcement of the obligation, moral and legal, devolved upon the husband to support his wife and to maintain and educate his children." (Emphasis added.)

The "fresh start" sanctioned by this early decision was to relieve a debtor from past debts which were dischargeable in bankruptcy. It is submitted that this is the very reason why the Petitioner, like other persons who are financially distressed, file for bankruptcy.

In *Burlingham v. Crouse*, 228 U.S. 459 (1913) a proviso of Section 70a of the Bankruptcy Act was interpreted to permit a bankrupt to retain a life insurance policy free from his creditors after he paid to the trustee the cash surrender value (which is all that could have been realized by the trustee for the creditors). The Court also considered the fresh start given the debtor as follows (at 473):

> "... It is the twofold purpose of the Bankruptcy Act to convert the estate of the bankrupt into

> cash and distribute it among creditors and then to give the bankrupt a *fresh start* with such exemptions and rights as the statute left untouched ... We think it was the purpose of Congress to pass to the trustee that sum which was available to the bankrupt at the time of bankruptcy, as a cash asset, otherwise to leave to the insured the benefit of his life insurance." (Emphasis added.)

In this context, a fresh start meant leaving the bankrupt with exempt property and the right to redeem his insurance policies under the proviso of Section 70a.

The Court decided that a discharge in bankruptcy covered the express obligation of a bankrupt's indemnification of his surety for any loss sustained upon a failure to perform a building contract. *Williams v. U. S. Fidelity Co.*, 236 U.S. 549 (1915). Even though the surety did not sustain the loss and pay the damages until after the bankruptcy petition had been filed, the indebtedness was discharged. In reaching this conclusion, the Court reasoned (at 554-555):

> "It is the purpose of the Bankruptcy Act to convert the assets of the bankrupt into cash for distribution among creditors and then to relieve the honest debtor from the weight of oppressive indebtedness and permit him to *start fresh* free from the obligation and responsibilities consequent upon business misfortunes. *Wetmore v. Markoe*, 196 U.S. 68, 77; *Zavelo v. Reeves*, 227 U.S. 625, 629; *Burlingham v. Crouse*, 228 U.S. 459, 473." (Emphasis added.)

The application of the "fresh start" doctrine was also referred to as "a new opportunity in life" in *Stellwagen v. Clum*, 245 U.S. 605 (1918), as follows (at 617):

"The federal system of bankruptcy is designed not only to distribute the property of the debtor not by law exempted, farily and equally among his creditors, but as a main purpose of the act, intends to aid the unfortunate debtor by giving him a fresh start in life, free from debts, except of a certain character, after the property which he owned at the time of bankruptcy has been administered for the benefit of creditors. Our decisions lay great stress upon this feature of the law – as one not only of private but of great public interest in that it secures to the unfortunate debtor, who surrenders his property for distribution, a new opportunity in life."

When *Local Loan Co. v. Hunt*, 292 U.S. 234 (1934), was decided, there was ample precedent by this Court that a bankrupt should not be denied a "fresh start" or new opportunity in life subsequent to his bankruptcy. However, the "fresh start" or "new opportunity in life" accorded a bankrupt upon discharge, as the cases discussed herein suggest, is not to the detriment of his creditors. All of those decisions recognize that the debtor's fresh start is conditioned upon a transfer of the property which he owned at the time of bankruptcy. unless exempt, to the trustee for the benefit of creditors.

In *Local Loan Co., supra*, this Court ruled that a state court could not enforce an assignment of *future* wages that had been made by the bankrupt prior to filing a petition in bankruptcy. In an unanimous decision, this Court reasoned (pp. 244-245):

"One of the primary purposes of the bankruptcy act is to 'relieve the honest debtor from the weight of oppressive indebtedness and permit him to *start afresh* free from the obligations and responsibilities

consequent upon business misfortunes.' *Williams v. U.S. Fidelity & G. Co.*, 236 U.S. 549, 554-555. This purpose of the act has been again and again emphasized by the courts as being of public as well as private interest, in that it gives to the honest but unfortunate debtor who surrenders for distribution the property which he owns at the time of bankruptcy, *a new opportunity in life and a clear field for future effort*, unhampered by the pressure and discouragement of preexisting debt. *Stellwagen v. Clum*, 245 U.S. 605, 617; *Hanover National Bank v. Moyses, supra; Swarts v. Fourth National Bank*, 117 Fed. 1, 3; *United States v. Hammond*, 104 Fed. 862, 863; *Barton Bros. v. Texas Produce Co.*, 136 Fed. 355, 357; *Hardie v. Swafford Bros. Dry Goods Co.*, 165 Fed. 588, 591; *Gilbert v. Shouse*, 61 F.2d 398. . . . When a person assigns future wages, he, in effect, pledges his future earning power. . . . *The new opportunity in life and the clear field for future effort*, which it is the purpose of the bankruptcy act to afford the emancipated debtor, would be of little value to the wage earner if he were obliged to face the necessity of devoting the whole or a considerable portion of his earnings for an indefinite time in the future to the payment of indebtedness incurred prior to his bankruptcy." (Emphasis added.)

The Court determined that an assignment of future wages made prior to bankruptcy could not be sanctioned because such wages are not property of the debtor at the time of bankruptcy.[35] In fact, the assignment of future wages was given by the debtor as

[35] 292 U.S. at 243.

security for a loan made by Local Loan Company to the debtor prior to bankruptcy, and the indebtedness was discharged in the bankruptcy proceeding. Obviously, the enforcement of the assignment, sought by the loan company in a post bankruptcy proceeding, would have frustrated the fundamental purpose of a bankruptcy discharge, namely to give the debtor a fresh start unencumbered with debts and obligations in existence at the time of bankruptcy.

While the Court has cited the "fresh start" doctrine for the purpose of upholding the bankrupt's right to future wages and freedom from pre-bankruptcy debts and obligations, it refused to apply the doctrine, in a very difficult factual situation. In *Legg v. St. John*, 296 U.S. 489 (1936), it was decided that the vested right of a bankrupt to receive disability benefits in the future under a paid-up insurance contract passed to the trustee in bankruptcy. Mr. Justice Brandeis, speaking for a unanimous court, observed (pp. 495-496):

> "[T]he obligation of the company to pay disability benefits in the future is not after-acquired property. It is property which was acquired by Legg long before the adjudication, and fully paid for by premiums paid before the adjudication. Nor are the benefits payable after the adjudication in any sense future earnings. They are not the fruit of anything to be done by Legg after the adjudication. The right to secure disability benefits in the future does not differ from any other right acquired before adjudication to receive money thereafter. It is in essence an annuity purchased and paid for prior to the adjudication. Like other property, it passed to the Trustee, unless exempted by the law of the bankrupt's domicile. The principle declared in *Local Loan Co. v. Hunt*, 292 U.S. 234, is not applicable here."

The Court noted (at 496-497) that Tennessee, the debtor's domicile, did not exempt disability benefits. The reference to the *Local Loan Co.* decision deserves some comment. Presumably the debtor argued that he was being denied a fresh start and that the disability benefits consituted after-acquired property. It is important to understand the distinction which Justice Brandeis made. Like an income tax refund, the disability benefits "are not the fruit of anything to be done" after bankruptcy and such benefits do not "differ from any other right acquired before bankruptcy to receive money thereafter." No doubt, this was a difficult decision to render because the effect was to deprive a disabled person of benefits which he obviously needed to purchase food, clothing and shelter. However, it was the correct decision because the Bankruptcy Act, then and now, requires that result.

In sum, it is clear that the "fresh start" doctrine, discussed in cases interpreting certain provisions of the Bankruptcy Act, including Section 70a is simply a characterization of the benefits flowing to the debtor after bankruptcy-relief from the obligation of pre-bankruptcy debts, retention of exempt property provided in Section 6 of the Act, and freedom to accumulate future wealth.

It is likewise clear that none of these cases, in any way, supports Petitioner's claim to an income tax refund derived from pre-bankruptcy wages. The various discharge benefits discussed in the cases are of no help to Petitioner. In fact, the holding of *Legg* not considered in Petitioner's brief, interprets the "fresh start" doctrine as inapplicable to a stituation in principle the same as the one presented herein.

B. *Segal v. Rochelle* and *Lines v. Frederick*.

As a general rule, an income tax refund due the bankrupt at the time of filing the petition has been considered as property within the meaning of Section 70a(5), except for two recent decisions.[36] These exceptions are a result of two lower courts' application and interpretation of two recent cases decided by this Court.

In *Segal v. Rochelle*, 382 U. S. 375 (1965) this Court determined that a refund arising out of a business loss incurred prior to bankruptcy was property owned by the bankrupt and "transferable" at the time that the bankruptcy petition was filed and, therefore, passed to the trustee, in accordance with §70a(5) of the Bankruptcy Act. In late 1961, voluntary bankruptcy petitions were filed by Gerald Segal, Sam Segal and their business partnership. After the close of 1961 (the taxable year of the loss), the trustee applied for income tax refunds for both of the individual bankrupts.[37] The operating losses underlying the refunds had been incurred by the partnership during that part of 1961 which was prior to the filing of the petitions in bankruptcy.[38] The losses were carried back to the years

---

[36]Calverly, *Income Tax Refunds Due Wage Earners*, J. of Nat. Assn. of Ref. in Bankruptcy 8, 10 (Jan. 1965). *Rev. Rul.* 72-38, 1972-2 CB 632; *In re Kingswood*, 343 F. Supp. 498, 504 (C.D. Calif. 1972). *In re Perry*, 225 F. Supp. 481 (N.D. Ohio 1963).

[37]Presumably, Applications for Tentative Carryback Adjustments (IRS Form 1139) were filed by the trustee. See Income Tax Regulations §1.6411-1(a) and (b).

[38]382 U.S. at 376.

1959 and 1960 to offset net income on which the Segals had both paid taxes.[39]

In examining Section 70a(5), the Court noted (at 379) that "[i]t is impossible to give any categorical definition to the word 'property' nor can we attach to it in certain relations the limitations which would be attached to it in others." According to the Court, the purposes of the Bankruptcy Act must govern whether an item is classed as "property."

The Court then reasoned (at 379):

> "[T]he main thrust of §70a(5) is to secure for creditors everything of value the bankrupt may possess in alienable or leviable form when he files his petition. To this end, the term 'property' has been construed most generously and an interest is not outside its reach because it is novel or contingent or because enjoyment must be postponed."

Further, the Court suggested (at 379):

> "However, limitations on the term do grow out of the purposes of the Act; one purpose which is highly prominent and is relevant in this case is to leave the bankrupt free after the date of his petition to accumulate new wealth in the future."

This purpose is illustrated by three examples: (1) future wages of the bankrupt; (2) inchoate right to a bequest or promised gift; and (3) an attorney's right to a contingent fee with respect to litigation pending at

---

[39]The refunds to Gerald Segal were in the amounts of $283.07 and $1,608.21 for the years 1960 and 1959, respectively; and the refunds to Sam Segal for 1960 and 1959 were $505.63 and $1,839.41, respectively.

the date of bankruptcy.[40] In each of these examples, on the date of bankruptcy, the debtor had no right to the asset in issue, and it has been recognized as fundamental to the Bankruptcy Act that the debtor's assets acquired after bankruptcy are not subject to debts and obligations dischargeable in bankruptcy. See *Local Loan Co. v. Hunt, supra.* The holding of *Segal* is entirely consistent with the earlier fresh start cases discussed herein.

The Court then concluded that the loss-carryback refund claim was "sufficiently rooted in the pre-bankruptcy past and so little entangled with the bankrupts' ability to make an unencumbered fresh start that it should be regarded as property under Section 70a(5)".[41] Subsequently, this phrase has been cited and applied by this Court in deciding whether layoff or vacation pay, accrued but unpaid at the time of bankruptcy, passed to the trustee as "property" under Section 70a(5).

In *Lines v. Frederick,* 400 U.S. 18 (1970), an employee of a large manufacturing company had accrued lay-off pay of $137.28 at the time he filed his petition. He could collect this sum either during the annual period when his employer shut down the plant in which he worked, or on final termination of his employment. Also involved in this case was another employee, who had accrued vacation pay of $144.14 which he could draw either on termination or under a conventional voluntary vacation plan of his employer.

In deciding that the lay-off and vacation pay was not property within the meaning of Section 70a(5), the

---

[40]382 U.S. at 379-380.

[41]*Id.* at 380.

Court inferred that the nature and relationship of the asset resembled future wages. The Court noted (at p. 20) that the debtors were wage earners whose sole source of income prior to and subsequent to bankruptcy was weekly earnings and that "the function of their accrued vacation pay is to support the basic requirements of life for them and their families during brief facation periods or in the event of layoff." Lastly, the Court suggested that "[T]he wage-earning bankrupt who must take a vacation without pay or forego a vacation altogether cannot be said to have achieved the 'new opportunity in life and [the] clear field for future effort, unhampered by the pressure and discouragement of pre-existing debt', ... *Local Loan Co. v. Hunt, supra.*, which it was the purpose of the statute to provide."

This Court in *Lines* recognized *vacation* pay as having a unique function in that it was related to a short and determinable period of non-labor which would occur *after* bankruptcy. The Court focused on the vacation as a necessary event associated entirely with the post-bankruptcy future. One of the debtors in *Lines* was in fact forced to take a vacation, occasioned by an annual two week shutdown of his employer's plant. In his dissenting opinion, Justice Harlan noted that if the employee lost the lay-off pay which had accrued to the date of bankruptcy, he would have had only three days' pay coming when his employer shut down the plant. Thus, the Court treated vacation pay as analogous to the future wages at issue in *Hunt*, noting that if the bankrupts were forced to live through a post-bankruptcy vacation or lay-off period without pay, they would lack a "clear field for future effort".

C. The conflicting holdings of *Cedor*, *Kokoszka* and *Gehrig*.

The *Segal* and *Lines* decisions formed the central basis for several recent conflicting decisions dealing with income tax refunds,[42] which this Court is to resolve by its decision herein. As previously noted, it has been the general practice to include in the bankrupt's estate income tax refunds due at the time of bankruptcy.[43] Since the *Segal* and *Lines* decisions, this practice has been under attack. The conflicting approaches taken by the Second, Eighth and Ninth Circuits can be summarized as follows:

1. *In re Cedor*,[44] the Ninth Circuit held that:

(a) The portion of a refund attributable to minimum[45] withholding does not pass to the trustee and can be retained by the Bankrupt.

---

[42]For general analysis and review of issues presented to this Court see Note, *The Income Tax Refund as a Possible Asset of a Wage Earner's Bankruptcy Estate*, 87 Harv. L. Rev. 395 (1973); Comment, *Title to Property - Employee Bankrupt's Income Tax Refunds*, 47 Am. Bankr. L.J. 239 (1973); Note, *Treatment of Income Tax Refunds in Bankruptcy After Lines v. Frederick*, 71 Mich L. Rev. 331 (1973); Note, *The Withholding Tax in the Bankruptcy Context*, _____ Brooklyn L. Rev. _____ (1974 - to be published).

[43]Note 36, *supra*.

[44]470 F.2d 996 (9th Cir. 1972).

[45]Minimum withholding means that the employee claimed the correct number of withholding exemptions on his IRS Form W-4 which he must execute upon beginning his employment. Income Tax Regulations, Section 31.3402(f)(2)-1. If his allowable exemptions increase during the course of his employment, he may execute another Form W-4; e.g., he marries, has a child, his itemized deductions increase, etc. See Section 3401(f)(1) of the Internal Revenue Code of 1954. The determination of the amount

(b) The portion of a refund attributable to optional[46] withholding is "property" which passes to the trustee pursuant to Section 70a(5), but only to the extent of 25% in accordance with the Consumer Credit Protection Act, Sections 1671-1677.

2. *In re Kokoszka,*[47] the Second Circuit ruled:

(a) An income tax refund, attributable to either minimum or optional withholding, is "property" within the meaning of Section 70a(5) and passes to the trustee.

---

of withholding was changed by the Revenue Act of 1971. Public Law 92-178, 92nd Cong., 1st Sess., §208 (1971). These changes have been codified as Section 3401(f), *supra.* The reason for the amendments was to enable wage earners to have the correct amount of income tax withheld and avoid both the over and under withholding. See H. Rept. No. 92-533, 92nd Cong., 1st Sess., 1972-1 Cum. Bull. 518-520. However, a wage earner may still claim fewer than the maximum withholding exemptions permitted him under the statute. Also, he may unconsciously cause his employer to over-withhold if his allowable deductions increase measurably during the tax year and he does not increase his withholding exemptions. For example, a married wage earner with an income under $8,000 should claim one additional withholding allowance for each $750 of deductions which exceed $1,700, the base figure in the withholding tables. Therefore if his allowable deductions during the year are between $1,701 and $2,450, he should claim one additional allowance; if the amount of such deductions are between $2,451 and $3,200, he should claim two additional exemptions. If the correct number of withholding exemptions are claimed, neither over nor under withholding will occur assuming the wage earner works the entire year.

[46]Optional withholding occurs when a taxpayer claims fewer than his permitted withholding exemptions. See Section 3401(f)(1), *supra.* This action results in more income tax being withheld than is necessary.

[47]479 F.2d 990 (2d. Cir. 1973).

(b) Since such tax refund is not "earnings" for the purposes of the Consumer Credit Protection Act, the entire refund, rather than only 25%, belongs to the trustee.

3. *In re Gehrig*,[48] the Eighth Circuit concluded that:

(a) The portion of a refund attributable to minimum withholding does not pass to the trustee and can be retained by the bankrupt.

(b) To the extent that a tax refund may be attributable to the optional withholding by the debtor, it is "property" within the meaning of Section 70a(5) and the provisions of the Consumer Credit Protection Act do not apply to any portion of such refund.

It is difficult, if not impossible, to perceive any basis for the distinction drawn by the Eighth and Ninth Circuits between optional and minimum withholding. Certainly, the language of Section 70a(5) makes no such distinction. It would seem to follow logically that if a refund is due at the time of bankruptcy with respect to taxes withheld from wages paid prior to bankruptcy, whether such refund is the result of optional or minimum withholding should not answer the question whether it is "property" under Section 70a(5). If the refund is "property" because the debtor had his employer over withhold, it follows that it is also "property" if the employee claims the correct number of withholding exemptions because the test depends upon whether the refund claim is transferable by the debtor at the date of bankruptcy, and not whether voluntarily withheld as "forced savings" or involuntarily withheld as required by law.

---

[48] 1974 CCH Bankruptcy Reports ¶65,116 (8th Cir. 1974).

D. Application of *Segal* and *Lines*.

As previously noted, there is nothing in the history or language of Section 70a to exclude a tax refund as "property". In fact, "it was the intent of Congress to secure to creditors all property of a bankrupt".[49] The laws of Connecticut do not exempt a tax refund as an exempt asset.[50] The tax refund is also assignable under Connecticut law.[51] Petitioner even admits that Connecticut law does not exempt wages.[52] Impliedly, Petitioner admits that the tax refund is not an exempt asset under the laws of the State of Connecticut; otherwise, there would be no reason to argue that this Court should decide that it is not "property" under Section 70a(5). In effect, this Court is being asked to create a Federal exemption that would exempt the tax refund, which tax refund would otherwise not be exempt under the laws of Connecticut.

In order for this Court to decide in Petitioner's favor, it must ignore the holding in *Legg v. St. John, supra*, as well as the meaning and application of Sections 70a(5) and 6 of the Bankruptcy Act. Moreover, the position urged by Petitioner would be extremely detrimental to the provisions of the practice under the Bankruptcy Act, because Sections 70a(5) and 6 would have a meaning wholly inconsistent with long standing interpretations by this Court and lower courts which must supervise bankruptcy proceedings daily.

---

[49] *Segal v. Rochelle*, at 379.

[50] See §52-352 of the laws of Connecticut.

[51] 479 F.2d at 993; this fact is not in dispute.

[52] Brief for Petitioner at 19-20.

Basically, Petitioner is requesting this Court to rest such a decision on the holding of *Lines v. Frederick, supra.* Petitioner's interpretation of the *Lines* decision disregards the meaning and application of the fresh start doctrine, and ignores the point that lay-off and vacation pay were considered by this Court equivalent to post-bankruptcy wages. Once Petitioner's analysis of *Lines* is rejected, he is left without any legal argument that the refund is not property under Section 70a(5). The following quote from the opinion of the Bankruptcy Judge ably explains the nature of an income tax refund and demonstrates why it is property within the meaning of Section 70a(5):

> "... First, wages are withheld under federal law for application on an eventual tax liability and are paid to and become the property of the government. Second, the wages are not withheld for taxes under any designed program that they or any portion of them shall be returned to the bankrupt to insure his future support when he is without daily earnings. Third, a claim to a refund arising out of taxes voluntarily or involuntarily paid out of wages is quite the equivalent of savings accumulated by a bankrupt out of his yearly earnings and any such savings held by a bankrupt at bankruptcy – whether in the form of cash in a safe deposit box or in a bank account – became the property of the bankruptcy estate. Fourth, a claim to a refund is not distinguishably different from any other property of property right which a bankrupt might have acquired by using a portion of his annual wages to make a loan to another, to buy securities or to acquire an automobile, all of which pass to a trustee in the event of bankruptcy. Accordingly, it is the view of this court that a claim to a tax refund for excess taxes paid from

wages is quite something different from a right to receive accumulated wages in the future which were specifically designed to substitute for future lack of earnings. The concept of *Lines* is not applicable to a tax refund. Such a refund is a property which passes to a trustee in bankruptcy under section 70a(5). (App, at 7-8).

Apart from ignoring the differences between an income tax refund and the accrued vacation pay at issue in *Lines*, Petitioner overemphasizes the importance that an income tax return has an origin in the bankrupt's wages and deserves special protection.

In support of this position, Petitioner cites *Sniadach v. Family Finance Corp.*, 395 U.S. 337 (1969); *James v. Strange*, 407 U.S. 128 (1972); *Fuentes v. Shevin*, 407 U.S. 67 (1972); *Lynch v. Household Finance Corp.* 405 U.S. 538 (1972), None of these causes concerned the issue presented before this Court. These respective decisions address other problems unassociated with the Bankruptcy Act and the interplay between Section 70a(5) and Section 6. Petitioner advanced the same argument before the Court of Appeals that wages are a specialized type of property. The appellate tribunal properly answered this contention as follows (p. 995):

> "... Just because some property interest had its source in wages, however, dos not give it special protection, for to do so would exempt from the bankrupt estate most of the property owned by many bankrupts, such as savings accounts and automobiles which had their origin in wages."

The Sixth Circuit was faced directly with the issue of whether wages earned prior to bankruptcy should be

given special protection under the Bankruptcy Act.[53] In that factual situation, the bankrupt had earned wages prior to bankruptcy which were unpaid at the date of his bankruptcy filing. The Sixth Circuit determined that wages not exempt under the laws of Ohio constitute property which should go to the trustee, relying upon the test set forth by this Court in *Segal v. Rochelle, supra,* and noted that the concept of a "fresh start" should not be judicially expanded to include "property" which would otherwise vest in the trustee.

Once *Lines* is limited to its own special facts, the criteria for including the income tax refund within the bankruptcy estate is whether the refund is "sufficiently rooted in pre-bankruptcy past", the tax refund in issue represented taxes withheld from wages earned by Petitioner prior to his filing for bankruptcy. The tax refund is not the equivalent of future wages and does not relate in any way to future wages.[54] At the end of each year, most wage earners must file a United States Income Tax Return.[55] Generally, the person either (1

---

[53] *In re Aveni,* 458 F. 2d 972 (6th Cir.), *cert. denied,* 409 U.S. 877 (1972).

[54] 379 U.S. at 375: "Accordingly, future wages of the bankrupt do not constitute property at the time of bankruptcy. . . . "

[55] An unmarried taxpayer with gross income in excess of $2,050.00 and married taxpayers, filing a joint return, with combined gross income in excess of $2,800.00 must file income tax returns. See Section 6012(a) of the Internal Revenue Code of 1954. However, those persons earning less may still file a return in order to claim a refund. This is what Petitioner did. He and his wife filed a joint return showing income of $2,322 and claimed a refund of the entire amount withheld from his wages ($250.90). Appendix, page 19.

pays no additional tax because the amount withheld equals the income tax due; (2) receives a tax refund because the amount withheld exceeds the income tax due; or (3) he must pay more tax because the income tax due exceeds the amount withheld. In the instant case, the bankrupt filed his petition on January 5, 1972, and at that time had a right to a refund for 1971 because he did not earn enough to pay any tax.[56] During 1971, Petitioner earned $2,322.00, and his employer withheld $250.90 based upon two withholding allowances claimed by the bankrupt.[57] On January 5, 1972, the date the bankruptcy petition was filed, Petitioner had a right to claim a refund from the United States Government for taxes paid during 1971.[58] It is apparent, therefore, that the refund of 1971 taxes is "sufficiently rooted in the pre-bankruptcy past" of Petitioner and certainly not "future wages" which would not be an asset of the bankrupt of the date of bankruptcy.

In *Segal*, this Court determined that transferring the tax claim to the trustee did not hinder the bankrupt from starting out on a "clean slate".[59]

---

[56]Mr. Kokoszka was employed for approximately three months during 1971. See Brief for Petitioner at 2.

[57]On or before the date an individual commences employment, he must execute a withholding exemption certificate (Form W-4), listing the number of withholding exemptions which he claims. See Section 3402(f)(2) of the Internal Revenue Code of 1954; Income Tax Regulations Section 31.3402(f)(2)-1. See Brief for Petitioner at 2-3.

[58]After December 31, 1971, Petitioner's 1971 taxable year ended, and he was then entitled to any refund for 1971. Petitioner filed a joint income tax return in mid-February 1972, and the refund check was received a short time later.

[59]382 U.S. at 380.

The Petitioner perceives "similarities"[60] between the accrued vacation issue in *Lines* and the tax refund question before this Court. The fact of the matter is that the income tax refund:

1. Relates solely to pre-bankruptcy earnings "sufficiently rooted in pre-bankruptcy past";[61]

2. It is not created out of "future wages"[62] but rather was withheld from pre-bankruptcy earnings;

3. Is a vested right in existence at the time of filing the petition;[63]

4. Is not an exempt asset under the laws of the State of Connecticut;[64]

5. Has traditionally been made available to creditors in accordance with long-standing practice throughout the bankruptcy courts of the United States;[65]

6. Does not deprive the Petitioner of a "fresh start" or "new opportunity in life" consistent with previous decisions.

If in 1971 Petitioner had loaned $250.59 to a third party and had gone into bankruptcy on January 5, 1972, (as he did), clearly that loan would have been a receivable due him and listed on Schedule B-2 (Personal Property) of his Bankruptcy Petition. It cannot be seriously questioned that this receivable would not have

---

[60]Brief for Petitioner at 8-10.

[61]*Segal v. Rochelle, supra.*

[62]*Local Loan Co. v. Hunt, supra.*

[63]Note 12, *supra.*

[64]Note 50, *supra.*

[65]Note 36, *supra.*

been an asset of the bankruptcy estate, i.e., "property" within the meaning of Section 70a(5). However, the effect of Petitioner's argument to this Court is that the loan receivable should not be deemed "property" because the debtor needs those funds for a "fresh start". Under this argument, the determination of what is "property" would be based on how much money the debtor needed in the future. It is suggested that the income tax refund in other cases could be as much as $1,000.[66]

The Bankruptcy Act objectives, "clean slate", "unencumbered fresh start", "new opportunity in life" and "clear field for future effort" enunciated in pre *Hunt cases, Hunt, Legg, Segal* and *Lines,* are not circumscribed by the tax refund going to the trustee. The discharge of Petitioner's $6,105.22 pre-bankruptcy unsecured debts, satisfies those objectives.

Certainly, Petitioner's income tax refund in the amount of $250.59 would help the debtor to pay for post bankruptcy medical or other expenses. However, the present Bankruptcy Act does not exempt "property" because the bankrupt could use money to pay personal expenses. The proposed Bankruptcy Act, discussed *infra* would permit Kokoszka, and other debtors, to retain up to $500 of an income tax refund.

---

[66]Brief for Petitioner at 17. On March 26, 1974, Donald C. Alexander, Commissioner of Internal Revenue, announced that the average refund was $345 for all tax returns processed to date. See "I.R.S. Expects to Step Up Tax Audits". New York Times (March 27, 1974).

III.

THE EXEMPTION OF THE INCOME TAX REFUND FROM THE BANKRUPT'S ESTATE IS BEING CONSIDERED BY THE CONGRESS.

A. Bankruptcy Commission.

There is pending before the Congress the most sweeping bankruptcy legislation since the Chandler Act was enacted in 1938.[67] On July 30, 1973, the Commission on the Bankruptcy Laws of the United States, pursuant to its legislative charter, transmitted to the President, the Chief Justice, and the Congress its Report, consisting of two principal parts, an analysis and evaluation of the present system of bankruptcy administration in the United States and recommendations for changes, including a new Bankruptcy Act.[68]

B. Legislative Recommendations.

The legislation, introduced in both Houses of the Congress and entitled the "Bankruptcy Act of 1973" was assigned to the Committees on the Judiciary in the House and Senate. As yet, neither Committee has held extensive hearings, and it is not expected that the legislation will be voted upon in either the House or the Senate by the end of this year. Presumably, the

---

[67]H.R. 10792, 93rd Cong., 1st Sess., introduced October 9, 1973; S. 2565, 93rd Cong., 1st Sess., introduced October 11, 1973.

[68]The Bankruptcy Commission was created by Senate Joint Resolution No. 88, 91st Congress (Public Law 91-354. July 24, 1970), and its members were appointed by the President, the Chief Justice, President of the Senate and Speaker of the House.

legislation will be reintroduced next year and considered by the Ninety-Fourth Congress.

In Chapter 7 of its Report, the Commission addresses the subject of exemptions and suggests that they are of particular importance to the consumer debtor.[69] The major complaint voiced by the Commission is that the present Act defers to state laws for what is exempt and this has resulted in a lack of uniformity of treatment of creditors and debtors.[70] It proposes to solve this problem by legislating the exemptions as a part of the new Bankruptcy Act. The following quote sums up the Commission's approach to exemptions:

> "The Commission recommends that kinds of property that traditionally have been treated as exempt by state governments form the nucleus of the federal exemptions with appropriate federal maximums. This approach avoids the unfairness of existing state exemptions laws, most of which are archaic, some of which are unduly generous and some of which are exceedingly niggardly, particularly as to urban residents. . . ."[71]

Specifically, the exemptions include, among other items not relevant, "Cash, securities, and receivables, including unpaid personal earnings, accrued vacation pay, and income tax refund, to the aggregate value of not more than $500.[72] In discussing the proposed statutory language, the Commission suggests that these assets,

[69]Report of the Commission on Bankruptcy Laws of the United States (hereinafter cited as Bankruptcy Report), Part I, at 169.

[70]*Id.*

[71]*Id.*, Part I, at 171.

[72]This provision is found in Section 4-503(c)(3) of H.R. 10792, *supra* note 67, at 120, and the same Section in S. 2565, *supra* note 67, at 114-115. Of course, it depends on the particular law of the state where the debtor resides whether an income tax refund is exempt. See Vukowich, *Debtor's Exemption Rights*, 62 Geo. L.J. 779, 829-830 (1974).

including an income tax refund, are often exempt under state laws.[73] Implicit in this analysis of the current Bankruptcy Act is that such asset is property within the meaning of Section 70a(5); otherwise, it would make no difference to propose to exempt it. Also, it must be stressed that the interpretation given the exemption provision of Section 6 is that state law governs whether an income tax refund is exempt. Both of these conclusions by the Commission are supported by the cases and legislative history cited earlier in the Brief.

The Report also recommends that "property of the estate" be defined in the proposed Bankruptcy Act and that "the tests of transferability and leviability under state law be abandoned."[74] Primarily, the Commission focuses on the requirement of the present Act that local law govern not only what is "property of the estate" but also the question whether property is voluntarily or involuntarily transferable.[75] The reference to state law to determine whether property is transferable, in the opinion of the Commission, is unnecessarily productive of litigation and produces a lack of uniformity.[76] The Commission interprets Section 70a(5) to cover property "which prior to the filing of the petition [the debtor] could by any means have transferred or which might have been levied upon and sold under judicial process against him, or otherwise seized, impounded, or sequestered".[77]

---

[73] Bankruptcy Report, Part II, at 128.

[74] *Id.*, Part I, at 17.

[75] *Id.*, Part I, at 193.

[76] *Id.*

[77] *Id.*

The proposed statutory language would streamline the definition of "property of the estate" as all property of the debtor as of the date of the petition, with exceptions not material herein, together with certain other property which can be recovered from third parties.[78] In any event, reference to state law, even under the proposed Bankruptcy Act, will still be necessary to determine what is the "property" of the debtor, and the Report suggests that "this reference has not proved too troublesome, and what difficulty it may create is far over-shadowed by the difficulty of codifying rules of property solely for the purpose of bankruptcy administration".[79]

After an exhaustive two year study of the present Bankruptcy Act, the Bankruptcy Commission, its staff and consultants, comprising the most knowledgeable and able bankruptcy scholars in the country, has concluded that the present Act does not produce uniformity, an essential ingredient of a national bankruptcy act, with respect to either what is "property of the estate" under Section 70a(5) or what property, which would otherwise be part of the bankruptcy estate, is exempt.[80] As discussed above, the answers to those questions hinge on the state laws of the jurisdiction where the debtor files his petition. The changes proposed by the Bankruptcy Commission would incorporate in the Bankruptcy Act itself the definition of "property of the estate" and the exemptions which would be allowed.

---

[78]Section 4-601(a) of H.R. 10792, *supra* note 67, at 135-137, and S. 2565, supra note 67, at 130-131.

[79]Bankruptcy Report, Part I, at 194.

[80]*Id.*, Part I, at 169, 193.

Certainly, the findings of the Bankruptcy Commission are entitled to great weight. The interpretation given Section 70a(5) of the Bankruptcy Act is that all property which could by any means have been transferred is property of the estate. This would include an income tax refund which could have been applied for by the debtor on the date of bankruptcy. Obviously, such an asset would not have been exempted by the Commission in the new Act unless it was property of the estate.[81]

In this proceeding, Petitioner is asking this Court to judicially amend the present Bankruptcy Act to either (1) determine that an income tax refund is not "property" within the meaning of Section 70a(5) or (2) decide than an income tax refund is "exempt" without reference to Section 6 of the Bankruptcy Act and the laws of Connecticut. It would seem that the exhaustive study and proposed Bankruptcy Act of the Commission on the Bankruptcy Laws of the United States, which is presently pending before the Congress, offers a more preferable and traditional way of considering amendments to the present Bankruptcy Act, and more particularly, when the changes sought by Petitioner would require a new approach to deciding what is "property" and what property is exempt, both fundamental questions under the Bankruptcy Act.

---

[81]The new definition of "property of the estate" combines in part, present Sections 70a(5) and (6) so that "property" for purposes of the new act would not be different with respect to covering an income tax refund. See Bankruptcy Report, Part II, 148-149.

IV.

THE CONSUMER CREDIT PROTECTION ACT DOES NOT PRECLUDE THE TRUSTEE FROM OBTAINING THE ENTIRE INCOME TAX REFUND WITHIN THE BANKRUPTCY ESTATE.

Petitioner contends[82] "that the income tax refund, even if it is 'property', is entitled to the 75% exemption enjoyed by all other wage payments under the provisions of the Consumer Credit Protection Act ("CCPA").[83] Petitioner bases his argument on Section 6 of the Bankruptcy Act, which does not affect the allowance to bankrupts of exemptions which are prescribed by the laws of the United States. Petitioner relies upon definitions contained in Section 1672 of the CCPA.[84] Petitioner argues that a tax refund is "earnings" because the refund consists entirely of compensation payable for personal services and that when the refund is returned to the Petitioner it is

[82]Brief for Petitioner at 28.

[83]15 U.S.C. §1671-1677.

[84]15 U.S.C. §1672. Definitions, provides:

"For the purposes of this subchapter:

(a) The term 'earnings' means compensation paid or payable for personal services, whether denominated as wages, salary, commission, bonus, or otherwise, and includes periodic payments pursuant to a pension or retirement program.

(b) The term 'disposable earnings' means that part of the earnings of any individual remaining after the deduction from those earnings of any amounts required by law to be withheld.

(c) The term 'garnishment' means any legal or equitable procedure through which the earnings of any individual are required to be withheld for payment of any debt."

"disposable" earnings because nothing is required by law to be deducted or withheld from these earnings. Petitioner, therefore, contends that the taking of the tax refund is a "garnishment" because the bankruptcy proceeding is a legal or equitable procedure through which the earnings of an individual are withheld for payment of a debt. These same contentions were asserted before the Appellate Court which held[85] that a tax refund is not "earnings" for the purposes of §1673 and therefore it is not protected by §1673.[86] The Appellate Court reasoned that the intent of the CCPA

---

[85] 479 F. 2d at 996-997. *In re Gehrig*, note 48, *supra*, concurred with the ruling of the 2nd Circuit and disagreed with *In re Cedar* note 44, *supra*, which held to the contrary.

[86] §1673. "Restriction on garnishment – Maximum allowable garnishment

(a) Except as provided in subsection (b) of this Section and in Section 1675 of this title, the maximum part of the aggregate disposable earnings of an individual for any workweek which is subjected to garnishment may not exceed

(1) 25 per centum of his disposable earnings for that week, or

(2) the amount by which his disposable earnings for that week exceed thirty times the Federal minimum hourly wage prescribed by Section 206(a)(1) of Title 29 in effect at the time the earnings are payable, whichever is less. In the case of earnings for any pay period other than a week, the Secretary of Labor shall by regulation prescribe a multiple of the Federal minimum hourly wage equivalent in effect to that set forth in paragraph (2).

Exceptions

(b) The restrictions of subsection (a) of this Section do not apply in the case of

(1) any order of any court for the support of any person.

(2) any order of any court of bankruptcy under chapter XIII of the Bankruptcy Act.

(3) any debt due for any State or Federal tax."

was to make certain that wage earners were able to receive at least 75% of their take home pay in any one period, so that they would have enough cash to meet basic needs. The Court concluded that it was clear from the language of Sections 1672 and 1673 and the legislative intent thereof, that "earnings" means periodic payments of compensation and does not pertain to every asset that is traceable in some way to such compensation.

Once again, legislative history is helpful in establishing the intent of Congress in enacting Title II "Garnishment" of the CCPA. In House Report No. 1040,[87] the Committee on Banking and Currency noted that restricting garnishment of wages had the following purposes:

> "Title II restricts the garnishment of wages, which the Committee finds to be a frequent element in the predatory extension of credit, resulting, in turn, in a disruption of employment, production and consumption."

In further analyzing the restriction of garnishment of wages embodied in Title II, the Committee stated at 1963:

> "While consumer credit has enjoyed phenomenal growth over the past twenty years, so have personal bankruptcies. Title II of your Committee's bill, restricting the garnishment of wages, will relieve many consumers from the greatest single pressure forcing wage earners into bankruptcies."

Additionally, in the Committee Report under the heading entitled, "What the Bill Would Do", the

[87] H. Rept. No. 1040, 90th Cong., 2nd Sess., 2 U.S. Code, Cong. & Adm. News, 1963 (1968).

Committee stated that "Title II is concerned with mitigating the harsh and burdensome effects on both employers and employees of the garnishment of employees' wages".[88] This statement further emphasizes that the Committee was notably concerned with the disruptive effects on employers and employees when an employee's wages were garnished by a creditor.

The Committee further reiterated its concern of employees' wages being garnished in that the Committee "finds that the garnishment of wages is frequently an essential element in the predatory extension of credit resulting in a disruption of employment, production, as well as consumption."[89] A further indication of the clear cut purpose of the garnishment restrictions is reflected by the Committee when it stated that: "Your Committee has adopted an amendment . . . prohibiting an employer from discharging an employee by reason of a single garnishment of the employee's wages."[90] Noting that Title II had received endorsement from trade unions and industrial groups, the Committee stated:

> "The limitations on the garnishment of wages adopted by your committee, while permitting the continued orderly payment of consumer debts, will relieve countless honest debtors driven by economic desperation from plunging into bankruptcy in order to preserve their employment and insure a continued means of support for themselves and their families."

---

[88] *Id.*, at 1966.

[89] *Id.*, at 1977.

[90] *Id.*, at 1978-1979.

It is apparent that the Committee was genuinely concerned about the undesirable consequences of unrestricted garnishments being placed with an employer which in turn could result "in economic desperation plunging an employee into bankruptcy".[91]

In addition to the intent of Congress expressed in the Committee Report, this same intent is clearly reflected in the Congressional findings and declaration of purposes in Section 1671(a)(1) and (2) of the CCPA.

> "(1) The unrestricted garnishment of compensation due for personal services encourages the making of predatory extensions of credit. Such extensions of credit divest money into excessive credit payments and thereby hinder the production and flow of goods in interstate commerce."
>
> "(2) The application of garnishment as a creditors' remedy frequently results in loss of employment by the debtor, and the resulting disruption of employment, production, and consumption constitutes a substantial burden on interstate commerce."

That "extensions of credit", "loss of employment", and "disruption of employment" refer to an ongoing employer-employee relationship is most apparent. Title II of the CCPA was intended to protect the employment of a debtor when his employer had been named in a garnishment proceeding and the employee's wages were sought to be garnished. The legislative history of the CCPA and the specific statutory language clearly manifest an intent to regulate garnishment in its usual and accepted sense – employer-employee relation-

---

[91] *Id.*, at 1979.

ship. Title II gives no suggestion that a different purpose was intended and there is nothing in the Act which provides or supports a contrary conclusion. If anything, the main objective of the CCPA was to keep wage earners out of bankruptcy and once bankruptcy has occurred, the CCPA was not intended to protect the bankrupt.

The Appellate Court correctly held that the Act was clearly intended to protect only compensation made in the form of periodic payments to support a wage earner's family and was not designed to pertain to every asset traceable to wage compensation. This is particularly true when a bankruptcy occurs since the income tax refund has no relationship to the bankrupt's receiving compensation directly from his employer in support of his family. An income tax refund does not fall within the definition of "earnings" or "disposable earnings".

Despite the fact that the trustee is "vested by operation of law with the title of the bankrupt as of the date of the filing of the petition initiating a proceeding", such a vesting is not within the definition of "garnishment", i.e., a "legal or equitable procedure through which earnings of any individual are required to be withheld for payment of any debt". Furthermore, the assertion by Petitioner that the Referee's turnover order comes within the CCPA requires little comment since such order is authorized and required by the provisions of the Bankruptcy Act, which provisions are directed at marshalling the assets of the bankrupt and not placing a garnishment with his employer. Finally, but most importantly, the overriding purposes of the

Bankruptcy Act are ignored by Petitioner.[92] If this Court accepts Petitioner's argument that the CCPA applies to a tax refund and thereby precludes the trustee from obtaining all of the refund, it will ignore the Bankruptcy Act.[93] There is nothing in the Bankruptcy Act which even remotely reflects such an intention, nor is there anything in the CCPA which likewise makes such an assumption.

---

[92]15 U.S.C. §1673(b)(2) provides: "The restrictions of subsection (a) of this Section do not apply in the case of . . . any order of any court of bankruptcy under Chapter XIII of the Bankruptcy Act." Chapter XIII of the Bankruptcy Act is designed to rehabilitate debtors through Wage Earners Plans, so that straight bankruptcy can be prevented. Since normally debtors would pay their creditors through their wages, the CCPA was designed not to affect this objective. There is nothing, however, to suggest that Congress intended to make applicable the CCPA to straight bankruptcy.

[93]Additionally, the Secretary of Labor's position (Petitioner's Brief, p. 36) is not supported by the history of the CCPA. Likewise, it is contrary to the basic provisions of the Bankruptcy Act.

CONCLUSION

For the foregoing reasons, the decision of the Circ
Court of Appeals should be in all respects affirmed.

Respectfully submitted,

BENJAMIN R. CIVILETTI
VENABLE, BAETJER AND
HOWARD
2 Hopkins Plaza
Baltimore, Maryland 2120
(301) 752-6780

Amicus Curiae

Of Counsel:

JAMES L. LEKIN
HARRY D. SHAPIRO
Venable, Baetjer and
Howard

IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1974

No. 73-5265

HENRY A. KOKOSZKA, Bankrupt,

Petitioner,

v.

RICHARD BELFORD, Trustee in Bankruptcy of the Estate of Henry A. Kokoszka, Bankrupt,

Respondent.

ON WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

PETITIONER'S REPLY BRIEF

JOANNE S. FAULKNER
169 Church Street
New Haven, Connecticut
JOSEPH DEAN GARRISON, JR.
FREDERICK W. DANFORTH, JR.
THOMAS R. ADAMS
JOHN T. HANSEN
MICHAEL H. WEISS

Attorneys for Petitioner

Washington, D.C. • CLB PUBLISHERS' • LAW PRINTING CO. • (202) 393-0625

TABLE OF CONTENTS

TABLE OF AUTHORITIES

IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1974

No. 73-5265

HENRY A. KOKOSZKA, Bankrupt,

Petitioner,

v.

RICHARD BELFORD, Trustee in Bankruptcy of the Estate of Henry A. Kokoszka, Bankrupt,

Respondent.

ON WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

PETITIONER'S REPLY BRIEF

Petitioner files this brief as permitted by Rule 41(5) to discuss new matter and by Rule 40(4) to reply to the Brief of Amicus Curiae for Respondent.

I.

GEHRIG V. SHREVES, DECIDED AFTER THE FILING OF PETITIONER'S BRIEF, DEALS WITH THE SAME ISSUES PRESENTED BY THIS CASE.

Gehrig v. Shreves is reported at 491 F.2d 668 (8th Cir. 1974).

A. The Eighth Circuit Properly Decided That The Income Tax Refund Is Not §70a(5) Property.

After close analysis of *Lines v. Frederick*, 400 U.S. 18 (1970) and *Segal v. Rochelle*, 382 U.S. 375 (1966), the Eighth Circuit concluded that an income tax refund attributable to minimum withholding is not property within the purview of §70a(5) of the Bankruptcy Act.

In so deciding, the Eighth Circuit agreed with the decision of the Ninth Circuit in *In re James*, 470 F. 2d 996 (1972), and rejected the Second Circuit's decision below as to that issue.

The court's analysis in *Gehrig* is remarkably similar to the position presented by petitioner in his main brief. Accordingly, petitioner will call the Court's attention to only two significant aspects of *Gehrig*.

First, the court made clear that in neither *In re Jones* 337 F. Supp. 620 (D. Minn. 1971) nor *In re Wetterhof*, 453 F. 2d 544 (8th Cir.) had it ruled on the issue of the income tax refund as property. Both cases were cited in the courts below to support their position (A. 22, 29). In view of the decision in *Gehrig*, neither case can now be cited as contrary to bankrupt's position here. *In re Kingswood*, also cited in the District Court and by the Amicus in this Court, has been reversed. 470 F.2d 996 (1972).

Second, the court concluded that as a matter of legal analysis and practical reality the tax refund check is a much future wages as the payments protected in *Lines*. "(A) low income wage earner must . . . spend all his funds on hand for personal and family sustenance whenever these funds become available."

B. The Eighth Circuit Incorrectly Concluded That The CCPA Does Not Protect A Bankrupt's Tax Refund Checks.

In *Gehrig v. Shreves*, 491 F.2d 668 (8th Cir. 1974), the court concluded that the portion of an income tax refund which represents optional withholding is, in effect, "savings". Since such a fund is savings, rather than "earnings" within the Consumer Credit Protection Act (CCPA), the court stated that the garnishment restrictions of the CCPA are not applicable.

It should be noted that the Eighth Circuit was referring only to the CCPA's application to optional overwithholding. The case presented in *Kokoszka* does not involve optional overwithholding, so that the "savings" analogy cannot be made.

Even so, the Bankrupt believes the Eighth Circuit was mistaken in stating that earnings when transformed into savings are not protected by the CCPA. The CCPA refers to compensation "paid or payable". 15 U.S.C. §1672(a). In such circumstances, this Court has held that payments retain their exempt quality even after deposit in a bank account. The test is whether the payments are subject to use for maintenance and support, and have not been converted into a permanent investment. *Philpott v. Essex County Welfare Board*, 409 U.S. 413, 416 (1973).

The agency charged with administering the CCPA has also concluded that, whether already paid or still payable, the wages retain their exempt character. (Petitioner's Brief, p. 37-38 and n. 15.)

Finally, nothing in the *Gehrig* record revealed voluntary excess withholding on the part of the bankrupt. Accordingly, the court's conclusion as to the inapplicability of the CCPA is dictum.

II.

THE DISPOSITION OF THIS CASE SHOULD NOT AFFECT THIS COURT'S DISPOSITION OF ANOTHER CASE ON ITS PRESENT DOCKET, *OTTE V. U.S.*

In re Freedomland, Inc., 480 F. 2d 184 (CA 2 1973) was cited by petitioner in support of the proposition that a bankrupt's personal tax refund check retains its original character as wages. (Petitioner's Brief pp.14, 29). This Court decided to reveiw *Freedomland* sub nom *Otte v. U.S.* Docket No. 73-375, 42 L.W. 3415 after the mailing of the Petitioner's Brief.

Two issues presented by *Freedomland* may be pertinent here. First, the *Freedomland* court decided that pre-bankruptcy funds of the bankrupt corporation to be paid by the trustee to the bankrupt's employees constitute wages as defined by the Internal Revenue Code. Thus far all the courts that have considered that point agree that the trustee's payments to the employees are wages. *U.S. v. Fogarty*, 164 F.2d 26, 29-32 (8th Cir. 1947); *U.S. v. Curtis*, 178 F.2d 268 (6th Cir. 1949); *Lines v. State Dept. of Employment*, 242 F.2d 201, 201-203 (9th Cir. 1957); In *Lines v. State Department of Employment, supra*, the Ninth Circuit stated:

> "The mere fact that the sums were actually paid to the employees by the Trustee does not deprive the payments of their primary identification as wages." *Id.* at 203.

The Ninth Circuit's holding in this regard is entirely consistent with their holding that a wage earner bankrupt's tax refund check constitute wages:

> "There does not appear to be any reason of policy why the amount of the refund should be

held to have lost its character as earnings by reason of its somewhat circuitous route to the wage earners hand." *In re Cedor*, 337 F. Supp. 1103, 1107. opinion adopted by the Ninth Circuit *sub nom. Riggs v. James*, 470 F.2d 996 (9th Cir. 1972), *cert den. sub. nom. Walsh v. Cedor*, 411 U.S. 973 (1973).

Other cases at issue in *Freedomland* tend to support Kokoszka's position herein that his tax refund check constitutes wages. In *Social Security Board v. Nierotko*, 327 U.S. 358 (1946) the Court held that a "back pay" award under the National Labor Relations Act should be treated as wages for purposes of eligibility for old age benefits under the Social Security Act. *Id.* at 364-66. In *Shropshire Woodliff & Co. v. Bush*, 204 U.S. 186, the Court held that an assignment of wages did not change the character of the payment to the assignee from wages.

The second issue in *Freedomland* possibly relevant herein in the distribution priority under 11 U.S.C. §104, of money to be paid to the Internal Revenue Service by the trustee of the bankrupt corporation as withholdings of the employee's wages. This court may decide that the proper priority is as costs and expenses of administration, wages, or taxes due and owing. However, the resolution of this issue should not affect the court's disposition of *Kokoszka* since the legal questions and policy issues are quite different.

Thus, it appears that the issues in *Freedomland* and *Kokoszka* are largely unrelated. To the extent the issues are similar, *Freedomland* and its companion cases tend to support Kokoszka's contention that his tax refund check constitutes wages.

III.

WELL ESTABLISHED PRINCIPLES DEMONSTRATE THAT THE BANKRUPT'S INCOME TAX REFUND IS NOT PROPERTY WITHIN THE MEANING OF THE BANKRUPTCY ACT; IT IS FUTURE WAGES UNDER THE HOLDING OF *LINES V. FREDERICK.*

The brief of amicus curiae for respondent presents a novel and highly conceptual approach to the issues herein. There the amicus argues that "property" is to be construed for the benefit of creditors, and the fresh start purpose of the Bankruptcy Act is adequately served by the provisions for the debtor's discharge and allowance of his exemptions. These points can best be understood by a brief re-examination of petitioner's presentation.

Kokoszka argues that the purpose of the Bankruptcy Act to give a debtor his fresh start places a limitation on the meaning of the word "property".

Noting that the Bankruptcy Act does not define the word property, Mr. Justice Harland stated in *Segal v. Rochelle*, 382 U.S. 375, 379:

> Whether an item is classed as "property" by the Fifth Amendment's Just Compensation Clause or for the purposes of a state taxing statute cannot decide hard cases under the Bankruptcy Act, whose own purposes must govern.

In *Lines v. Frederick*, 400 U.S. 18, this court noted that "The most important consideration limiting the breadth of the definition of 'property' lies in the basic purpose of the Bankruptcy Act to give the debtor a [fresh start]." *Id.* at 19. The other prominent purpose of the Bankruptcy Act is to secure property for the bankrupt's creditors. *Segal v. Rochelle, supra.*

In the case herein, Kokoszka contends that application of this analysis to his income tax refund should result in a holding that the refund check is not property because it is as much future wages as the vacation pay in *Lines*. The "elements" of *Lines* are set forth in Petitioner's brief pp. 8-10, and those same elements are present here. Furthermore, Petitioner's brief demonstrates that the refund is a planned on annually recurring event as much a part of a family's basic budget as vacation pay. *In re Cedor*, 337 F. Supp. 1103, 1105; *Gehrig v. Shreves, supra.* Nor has it been created as the result of any "investment", loan, or voluntary act by the bankrupt. But for legally mandated withholding, these wages would have been available when paid and would have been used for Kokoszka's support. Mr. Blackmun made the same point in a dissenting opinion:

> "Were it not for the withholding scheme the amounts would have been paid out to the employees as gross wages". *U.S. v. Randall*, 401 U.S. 513, 518.

It is the Internal Revenue Code and not action by the bankrupt which has turned these wages into "future wages". Furthermore the bankrupt herein is not contending that *Lines* should apply to property interests traceable to wages. The Bankrupt argues that the refund check *is* future wages under the holding of *Lines*.

Thus, although the theory of the amicus brief that the word property should only be construed for the benefit of creditors is novel, the Court has in fact adopted a broader approach of defining the word by reference to the purposes of the Bankruptcy Act. See *Local Loan v. Hunt*, 292 U.S. 234; *Segal v. Rochelle*,

supra; Lines v. Frederick, supra; and *Perez v. Campbell*, 402 U.S. 637. If the Court accepts the amicus' argument that the purpose of the Bankruptcy Act to give a debtor a fresh start does not impose a limitation on the meaning of the word property in the Bankruptcy Act, it would amount to overruling the approach, if not the result, of all these cases. Such an extreme departure is unwise and unwarranted not in the least because it would re-open a vast array of legal problems which are not regarded as settled.

The second aspect of the amicus' theory is that the only property to be retained by the bankrupt is exempt property. (Brief of Amicus pp. 11-20). Aside from the fact that this analysis begs the central question of the scope and meaning of the word property, it is also entirely without support. This Court has never refrained from an analysis of the definition of property because the asset in question was protected by an exemption statute. In *Legg v. St. John*, 296 U.S. 489, 491, a case emphasized by the amicus, this court noted that the monthly disability payments in question were partially exempt as income, but then went on to analyze whether the remainder was "property". Most recently in *Lines v. Frederick, supra,* this Court noted that vacation pay was partially exempt under California law. (*Id.* at 18); but, nevertheless, held that the remainder was not property within the meaning of the Bankruptcy Act.

Apparently, the amicus urges this limited application of the "fresh start" doctrine because he feels that such a limited application "is not to the detriment of [a bankrupt's] creditors". (Brief of Amicus Curiae pp. 22-23) However, at no point in his brief did the amicus for the trustee even attempt to rebut the bankrupt's substantial evidence that a ruling in the bankrupt's

favor will not be to creditor's detriment. (Petitioner's Brief p. 18).

F[illegible] amicus misconstrues the bankrupt's pc[illegible]esting that this Court is being asked to judici[illegible] a new federal exemption. The Bankrupt herein [illegible] only to have this Court engage in its traditional function of interpreting federal statutes: namely, the use of the word property in the Bankruptcy Act. The bankrupt's presentation is that ordinary legal analysis and the practical realities of the situation compel a decision in his favor.

Nor need the Court be deterred by the possibility of the revision of the Bankruptcy Law. As the bankrupt pointed out in his opening brief, and as the amicus seems to acknowledge, the findings of the Commission would support a holding by this Court that the refund check is not property. Similarly in *Snaidach v. Family Finance, supra,* the CCPA was enacted, but not yet effective. The Court in *Snaidach* found the policies of the CCPA supported that decision rather than favoring abstention. The same considerations apply to this case.

IV.

LEGG V. ST. JOHN IS INAPPLICABLE TO THE FACTS OF THIS CASE AND SHOULD BE REGARDED AS OVERRULED.

Legg v. St. John, 296 U.S. 489 is relied on extensively by the amicus for respondents (Brief of Amicus Curiae pp. 24-25, 35). In *Legg* a totally and permanently disabled bankrupt was entitled to receive monthly disability benefits as a supplementary benefit under his life insurance policy. Most of those benefits were not exempt. The Court held that these benefits were property that passed to the trustee.

Initially the *Legg* case is distinguishable from *Kokoszka* in two important respects. First, the Court determined the disability benefits as paid-up insurance. *Id.* at 495. Since it was a voluntary investment, the fund in *Legg* differs markedly from the involuntary nature of the tax refund check which is not in any respect an "investment". Additionally, in *Legg* the Court found that the benefits in question were not earnings; whereas the refund check in question here is nothing else but earnings.

Nevertheless, *Legg* is a harsh and unusual departure from the line of decisions by this Court interpreting the fresh start doctrine. Because Legg was permanently disabled, his ability to be "free from the burden of past debt and free to accumulate new wealth" depended upon receipt of his disability payments. It makes no difference to the bankrupt if his creditors obtain his non-exempt disability benefits through execution or if the bankruptcy trustee obtains it under §70. To Legg bankruptcy provides no protection and no fresh start. There the decision of this Court left Legg utterly trapped in the pauperism which the Bankruptcy Act was designed to relieve.

Legg v. St. John has never been cited or followed by this Court since it was decided. In light of *Lines v. Frederick* and *Perez v. Campbell*, it should properly be regarded as overruled. *Legg* is also inconsistent with the modern approach of this Court as stated in *Goldberg v. Kelly*, 397 U.S. 254 (1970); *California Department of H.R.D. v. Java*, 402 U.S. 121 (1971); *Snaidach v. Family Finance*, 395 U.S. 337 (1969); *James v. Strange*, 407 U.S. 128 (1972); *Philpott v. Essex County Welfare Board*, 409 U.S. 413 (1973); *U.S. v. Kras*, 409 U.S.

435* (1973). In any event, it is a highly unusual departure from a long chain of decisions of this Court and it interprets the Bankruptcy Act in such a harsh, legalistic way so as to deprive it of its central purpose. Thus, because *Legg* is an aberration, because it was wrongly decided, and because it has been overruled by implication, it should not be resurrected now and extended to apply to Kokoszka.

V.

THE EXEMPTION GRANTED BY THE CCPA IS APPLICABLE IN BANKRUPTCY.

In connection with the "property" question, the amicus for respondent argued that exemptions are important to the statutory scheme of bankruptcy. Despite his emphasis on the importance of exemptions to the bankrupt, the amicus for the trustee argues that the CCPA is not applicable even though exemptions "prescribed by the laws of the United States" are recognized by Section 6 of the Bankruptcy Act. The bankrupt's position herein is that the CCPA applies both by the terms of the Bankruptcy Act in §6 and by the terms of the CCPA itself.

The amicus relies principally on the legislative history of the Consumer Credit Protection Act (CCPA) to

---

*[C]ongressional concern for the debtor, [is] apparent from the provisions permitting the debtor to file his petition without payment of any fee, with consequent freedom of subsequent earnings and of after-acquired assets (with the rare exception specified in §70(a) of the Act), . . . from the claims of then existing obligations. These provisions . . . enable a bankrupt . . . to protect his future earnings and property, and to have his new start with a minimum of effort and financial obligation. *Id.* at 448-9.

support his argument that the CCPA is not applicable to a bankrupt's income tax refund. His position is that the legislative intent behind the CCPA was to prevent wage earners from being forced into bankruptcy by protecting their wages from excessive garnishment. But the prevention of bankruptcies was not the exclusive motivating force behind the CCPA. There is also the expressed intent to establish uniform bankruptcy laws. This presumes bankruptcy has occurred. [15 U.S.C. §1671(a) (3) and (b)]. Uniformity is effected by the application of the CCPA garnishment restriction to the previously varied state wage exemptions.** In this light, the reference to Chapter XIII orders of the Bankruptcy Court, [15 U.S.C. §1673(b) (2)], clearly presupposes the CCPA's applicability to bankruptcy proceedings.

Congress may not have adverted to the peculiar situation of the income tax refund when it adopted the CCPA. However, the natural reading of the statutory language encompases the refund. "[I]f Congress has made a choice of language which fairly brings a given situation within a statute, it is unimportant that the particular application may not have been contemplated by the legislators." *Barr v. U.S.*, 324 U.S. 83, 90 (1944); *Daniel v. Paul*, 395 U.S. 298, 307 (1969); *NLRB v. Plasterer's Local Union*, 404 U.S. 116, 128-29 (1971).

The definition of earnings includes all forms of compensation for personal services, whether periodic in nature or not. As argued in petitioner's brief, other

---

**In at least one prominent bankruptcy jurisdiction, the portion of the refund attributable to earnings within the 30 day period prior to bankruptcy was considered exempt under the wage exemption there applicable. *In Re James*, 470 F.2d 996 (9th Cir. 1972) (Record p. 5).

provisions of the CCPA also support its application to the income tax refund; and so do the interpretations of the administering agency.

Here again, the trustee misstates the bankrupt's position. There is no contention that the CCPA applies to every asset traceable to wages. The refund is directly and specifically part of wages. *E.g., U.S. v. Randall*, 401 U.S. 513, 518 (dissent by Blackmun, J.) For the trustee to take it would have a "harsh and burdensome effect" on the wage earning employee. H. Rep. No. 1040, 2 U.S. Cond Cong. & Adm. News 1966 (1968).

The trustee next argues that his taking of the refund is not the type of garnishment with which Congress was concerned. But again, the statutory definition is not restricted to the traditional concept of garnishment. It expressly includes any legal or equitable procedure. *Hodgson v. Christopher*, 365 F. Supp. 583, 586-87 (D.N.D. 1973); *Philpott v. Essex County Welfare Board*, 409 U.S. 413 (1973); Petitioner's Brief, p. 31-34.

CONCLUSION

For the reasons stated herein, and in Petitioner's Brief, this Court is respectfully requested to reverse the ruling of the Second Circuit Court of Appeals.

JOANNE S. FAULKNER
New Haven Legal Assistance
Association, Inc.
169 Church Street
New Haven, Connecticut 06510
(203) 772-3340

Counsel for Petitioner

JOSEPH DEAN GARRISON, JR.
FREDERICK W. DANFORTH, Jr.
New Haven Legal Assistance
Association, Inc.
THOMAS R. ADAMS
Legal Aid Society of
San Mateo County
7324 Mission Street
Daly City, California 94104
(415) 755-8550
JOHN T. HANSEN
MICHAEL H. WEISS
Hansen, Jaffe & Weiss
555 Polk Street, Suite 201
San Francisco, California 94102
(415) 771-5281

(Slip Opinion)

NOTE: Where it is feasible, a syllabus (headnote) will be released, as is being done in connection with this case, at the time the opinion is issued. The syllabus constitutes no part of the opinion of the Court but has been prepared by the Reporter of Decisions for the convenience of the reader. See *United States* v. *Detroit Lumber Co.*, 200 U.S. 321, 337.

SUPREME COURT OF THE UNITED STATES

Syllabus

KOKOSZKA *v.* BELFORD, TRUSTEE IN BANKRUPTCY

CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

No. 73–5265. Argued April 22, 1974—Decided June 19, 1974

1. An income tax refund is "property" that passes to the trustee under § 70 (a) (5) of the Bankruptcy Act, being "sufficiently rooted in the bankruptcy past," and not being related conceptually to future wages for the purpose of giving the bankrupt wage earner a "fresh start." *Lines* v. *Frederick*, 400 U. S. 18, distinguished. Pp. 3–7.

2. The provision in the Consumer Credit Protection Act limiting wage garnishment to no more than 25% of a person's aggregate "disposable earnings" for any pay period does not apply to a tax refund, since the statutory terms "earnings" and "disposable earnings" are confined to "periodic payments of compensation and [do] not pertain to every asset that is traceable in some way to such compensation." Hence, the Act does not limit the bankruptcy trustee's right to treat the tax refund as property of the bankrupt's estate. Pp. 7–10.

479 F. 2d 990, affirmed.

BURGER, C. J., delivered the opinion for a unanimous Court.

SUPREME COURT OF THE UNITED STATES

No. 73–5265

Henry A. Kokoszka, Petitioner, *v.* Richard Belford, Trustee, Etc.

On Writ of Certiorari to the United States Court of Appeals for the Second Circuit.

[June 19, 1974]

MR. CHIEF JUSTICE BURGER delivered the opinion of the Court.

We granted certiorari in this case to resolve the conflict among the courts of appeals on the questions of whether an income tax refund is "property" under § 70 (a)(5) of the Bankruptcy Act [1] and whether, assuming that all or part of such tax refund is property which passes to the trustee, the Consumer Credit Protection Act's [2] limitation

[1] The pertinent parts of § 70 (a)(5) of the Bankruptcy Act, 11 U. S. C. § 110 (a)(5), read as follows:

"(a) The trustee of the estate of a bankrupt . . . shall . . . be vested by operation of law with the title of the bankrupt as of the date of the filing of the petition initiating a proceeding under this title . . . to all of the following kinds of property wherever located . . . (5) property, including rights of action, which prior to the filing of the petition he could by any means have transferred or which might have been levied upon and sold under judicial process against him, or otherwise seized, impounded, or sequestered . . . ."

It is undisputed that the refunds could have been transferred under Connecticut law at the time of the filing of the petition, cf. *Segal* v. *Rochelle*, 382 U. S. 375, 381–385 (1966).

[2] 82 Stat. 146, 15 U. S. C. § 1601 *et seq.*

on wage garnishment serves to exempt 75% of the refund from the jurisdiction of the trustee.[3]

The petitioner was employed for the first three months of 1971. He was then unemployed from April 1971 until late in December of that year. He was re-employed for about the last week and a half of December 1971. While employed, petitioner claimed two exemptions for federal income tax purposes, the maximum number of deductions to which he was entitled, and his employer withheld the appropriate portion of his wages. 26 U. S. C. § 3402. During the year 1971, petitioner had a gross income of $2,322.

On January 5, 1972, petitioner filed a voluntary peti-

---

[3] 15 U. S. C. § 1673 reads, in pertinent part:

"Maximum allowable garnishment

"(a) Except as provided in subsection (b) of this section and in section 1675 of this title, the maximum part of the aggregate disposable earnings of an individual for any workweek which is subjected to garnishment may not exceed

"(1) 25 per centum of his disposable earnings for that week, or

"(2) the amount by which his disposable earnings for that week exceed thirty times the Federal minimum hourly wage prescribed by Section 206 (a)(1) of Title 29 in effect at the time the earnings are payable,

"whichever is less. In the case of earnings for any pay period other than a week, the Secretary of Labor shall by regulation prescribe a multiple of the Federal minimum hourly wage equivalent to that set forth in paragraph (2).

"Exceptions

"(b) The restrictions of subsection (a) of this section do not apply in the case of

"(1) any order of any court for the support of any person.

"(2) any order of any court of bankruptcy under chapter XIII of the Bankruptcy Act.

"(3) any debt due for any State or Federal tax.

"Execution or enforcement of garnishment order or process prohibited

"(c) No court of the United States or any State may make, execute, or enforce any order or process in violation of this section."

tion in bankruptcy. With the exception of a 1962 Corvair automobile which the Trustee abandoned as an asset upon the bankrupt's payment of $25, the sole asset claimed by the Trustee in bankruptcy was an income tax refund check for $250.90. On February 3, 1972, the Referee in Bankruptcy entered an *ex parte* order directing petitioner to turn this check over to the Trustee upon its receipt. The bankrupt moved to vacate that order and, after a hearing, the Referee denied the motion. In mid-February 1972, petitioner filed his income tax return for the calendar year 1971. Several weeks later, he received his refund check from the Internal Revenue Service. Upon its receipt, petitioner complied with the order of the Trustee but filed a petition for review of the Referee's decision in the United States District Court.[4] The District Court denied relief. Petitioner was granted leave to appeal.[5] On May 18, 1973, the United States Court of Appeals, Second Circuit, affirmed the order of the District Court, holding that the tax refund was property within the meaning of § 70a (5) of the Bankruptcy Act and that it therefore vested in the Trustee. The court further held that the limitations on garnishment contained in the Consumer Credit Protection Act did not apply to bankruptcy situations and that, consequently, the Trustee was entitled to the entire refund. Petitioner seeks review of these questions here.

(1)

We turn first to the question of whether petitioner's income tax refund was "property" within the meaning of § 70a (5) of the Bankruptcy Act. The term has never been given a precise or universal definition. On an earlier occasion, in *Segal* v. *Rochelle*, 382 U. S. 375 (1965), the Court noted that " '[i]t is impossible to give

[4] 11 U. S. C. § 67c.
[5] 11 U. S. C. § 47a.

any categorical definition to the word 'property' nor can we attach to it in certain relations the limitations which would be attached to it in others." *Id.*, at 379, quoting *Fisher* v. *Cushman*, 103 F. 860, 864 (1900). In determining the term's scope—and its limitations—the purposes of the Bankruptcy Act "must ultimately govern." *Id.*, at 379. See also *Lines* v. *Frederick*, 400 U. S. 18 (1970); *Local Loan Co.* v. *Hunt*, 292 U. S. 234 (1934).

In applying these general considerations to the present situation, there are some guidelines. In *Burlingham* v. *Crouse*, 228 U. S. 459 (1913), for example, the Court stated:

> ". . . It is the twofold purpose of the Bankruptcy Act to convert the estate of the bankrupt into cash and distribute it among creditors and then to give the bankrupt a fresh start with such exemptions and rights as the statute left untouched." *Id.*, at 473.

See also *Wetmore* v. *Markoe*, 196 U. S. 68, 77 (1904); *Williams* v. *U. S. Fidelity Co.*, 236 U. S. 549, 554–555 (1915); *Stellwagen* v. *Clum*, 245 U. S. 605, 617 (1918). On two rather recent occasions, the Court has applied these general principles to the precise statutory section and to the precise term at issue here. In *Segal* v. *Rochelle*, *supra*, the Court said:

> "The main thrust of § 70a (5) is to secure for creditors everything of value the bankrupt may possess in alienable or leviable form when he files his petition. To this end the term 'property' has been construed most generously and an interest is not outside its reach because it is novel or contingent or because enjoyment must be postponed." 382 U. S., at 379.

At the same time, the Court noted that this construction must be tempered by the intent of Congress "to leave

the bankrupt free after the date of his petition to accumulate new wealth in the future," *id.*, at 379, and thus "make an unencumbered fresh start." *Id.*, at 380. Several years later, in *Lines* v. *Frederick*, *supra*, these same considerations were repeated in almost identical language. 400 U. S., at 19. *Segal* and *Lines*, while construing § 70a (5) in almost identical language, reached contrary results. In each case, the Court found the crucial analytical key not in an abstract articulation of the statute's purpose but in an analysis of the nature of the asset involved in light of those principles.

In *Segal*, *supra*, this Court held that a business generated loss carryback tax refund—which was based on prebankruptcy losses but received after bankruptcy—should pass to the trustee as § 70a (5) property. Balancing the dual purpose of the Bankruptcy Act, see *Burlingham* v. *Crouse*, *supra*, the Court concluded that the refund was "sufficiently rooted in the prebankruptcy past and so little entangled with the bankrupt's ability to make an unencumbered fresh start that it should be regarded as 'property' under § 70a (5)," 382 U. S., at 380. The Court noted that "the very losses generating the refunds often help precipitate the bankruptcy and injury to the creditors," *id.*, at 378, and that passing the claim to the Trustee did not impede a "fresh start." On the contrary, a bankrupt "without a refund claim to preserve has more reason to earn income rather than less." *Id.*, at 380.

In *Lines*, *supra*, on the other hand, the Court held that vacation pay, accrued prior to the date of filing and collectible either during the plant's annual shutdown for vacation or on the final termination of employment, does not pass to the Trustee as § 70a (5) property. As in *Segal*, *supra*, the Court analyzed the nature of the asset in the light of the dual purposes of the Bankruptcy Act. It concluded that such vacation pay was closely tied to

the bankrupt's opportunity to have a "'clear field for future effort, unhampered by the pressure and discouragement of preexisting debt.'" 400 U. S., at 20, quoting *Local Loan Co.* v. *Hunt*, *supra*.

The income tax refund at issue in the present case does not relate conceptually to future wages and it is not the equivalent of future wages for the purpose of giving the bankrupt a "fresh start." The tax payments refunded here were income tax payments withheld from the petitioner prior to his filing for bankruptcy and are based on earnings prior to that filing. Relying on *Lines*, however, petitioner contends that the refund is necessary for a "fresh start" since it is solely derived from wages. In *Lines*, we described wages as "a specialized type of property presenting distinct problems in our economic system"[6] since they provide the basic means for the "economic survival of the debtor." *Id.*, at 20.

Petitioner is correct in arguing that both this tax refund and the vacation pay in *Lines* share the common characteristic of being "waged based." It is also true, however, that only the vacation pay in *Lines* was designed to function as a wage-substitute at some *future* period and, during that *future* period, to "support the basic requirements of life for [the debtors] and their families . . . ." *Ibid.* This distinction is crucial. As the Court of Appeals noted, since a "tax refund is not the weekly or other periodic income required by a wage earner for his basic support, to deprive him of it will not hinder his ability to make a *fresh* start unhampered by the pressure of preexisting debt," 479 F. 2d, at 994. (1973). "Just because some property interest had its source in wages . . . does not give it special protection, for to do so would exempt from the bankrupt estate most

[6] 400 U. S., at 20, quoting *Sniadach* v. *Family Finance Corp.*, 395 U. S. 337, 340 (1969).

of the property owned by many bankrupts, such as savings accounts and automobiles which had their origin in wages." *Id.*, at 995.

We conclude, therefore, that the Court of Appeals correctly held that the income tax refund is "sufficiently rooted in the bankruptcy past" [7] to be defined as "property" under § 70a (5).

(2)

Our disposition of the first issue requires that we turn next to the petitioner's contention that 75% of the refund is exempt under the provisions of the Consumer Credit Protection Act. The Act provides that no more than 25% of a person's aggregate disposable earnings [8] for any workweek or other pay period may be subject to garnishment. A trustee in bankruptcy takes title to the bankrupt's property "except insofar as it is property which is held to be exempt. . . ." Bankruptcy Act, § 70 (a), 11 U. S. C. § 110 (a). Another section provides that the Act "shall not affect the allowance to bankrupts of the exemptions which are prescribed by the laws of the United States. . . ." Bankruptcy Act § 6, 11 U. S. C. § 24. Petitioner argues the Consumer Credit Protection Act's restrictions on garnishment, 15 U. S. C. § 1671

[7] *Segal, supra,* at 380.

[8] C. C. P. A., 15 U. S. C. § 1672, entitled, "Definitions," states: "For the purpose of this subchapter:

"(a) The term 'earnings' means compensation paid or payable for personal services, whether denominated as wages, salary, commission, bonus, or otherwise, and includes periodic payments pursuant to a pension or retirement program.

"(b) The term 'disposable earnings' means that part of the earnings of any individual remaining after the deduction from those earnings of any amounts required by law to be withheld.

"(c) The term 'garnishment' means any legal or equitable procedure through which the earnings of any individual are required to be withheld for payment of any debt."

et seq., are such an exemption. In essence, the petitioner's position is that a tax refund, having its source in wages and being completely available to the taxpayer upon its return without any further deduction, is "disposable earnings" within the meaning of the statute. 15 U. S. C. § 1672 (a)(b). He further argues that the taking of custody by the Trustee is a "garnishment" since a bankruptcy proceeding is a "legal or equitable procedure[s] through which the earnings of any individual are required to be withheld for payment of any debt." 15 U. S. C. § 1672 (c).

The Congress did not enact the Consumer Credit Protection Act in a vacuum. The drafters of the statute were well aware that the provisions and the purposes of the Bankruptcy Act and the new legislation would have to coexist. Indeed, the Act explicitly rests on both the bankruptcy and commerce powers of the Congress. 15 U. S. C. § 1671 (b). We must therefore take into consideration the language and purpose of both the Bankruptcy Act and the Consumer Credit Protection Act in assessing the validity of the petitioner's argument. When "interpreting a statute, the court will not look merely to a particular clause in which general words may be used, but will take in connection with it the whole statute (or statutes on the same subject) and the objects and policy of the law, as indicated by its various provisions, and give to it such a construction as will carry into the execution the will of the Legislature. . . ." *Brown* v. *Duchesne*, 60 U. S. 183, 194 (1857).

An examination of the legislative history of the Consumer Protection Act makes it clear that, while it was enacted against the background of the Bankruptcy Act, it was not intended to alter the clear purpose of the latter Act to assemble, once a bankruptcy petition is filed, all of the debtor's assets for the benefit of his creditors. See, *e. g.*, *Segal*, *supra*. Indeed, Congress'

concern was not the *administration* of a bankrupt's estate but the *prevention* of bankruptcy in the first place by eliminating "an essential element in the predatory extension of credit resulting, in turn, in a disruption of employment, production, as well as consumption" [9] and a consequent increase in personal bankruptcies. Noting that the evidence before the Committee "clearly established a casual connection between harsh garnishment laws and high levels of personal bankruptcies," [10] the House Report concluded:

> "The limitations on the garnishment of wages adopted by your committee, while permitting the continued orderly pay of consumer debts, will relieve countless honest debtors driven by economic desperation from plunging into bankruptcy in order to preserve their employment and insure a continued means of support for themselves and their families." H. R. Rep. No. 1040, 90th Cong., 1st Sess., 21. See also p. 7.

In short, the Consumer Credit Protection Act sought to prevent consumers from entering bankruptcy in the first place. However, if, despite its protection, bankruptcy did occur, the debtor's protection and remedy remained under the Bankruptcy Act.

The Court of Appeals held that the terms "earnings" and "disposable earnings" as used in 15 U. S. C. §§ 1672, 1673, did not include a tax refund, but were limited to "periodic payments of compensation and [do] not pertain to every asset that is traceable in some way to such compensation." 479 F. 2d, at 997. This view is fully supported by the legislative history. There is every indication that Congress, in an effort to avoid the necessity of bankruptcy, sought to regulate garnishment in

[9] H. R. Rep. No. 1040, 90th Cong., 1st Sess., 20.
[10] *Id.*, at 20–21.

its usual sense as a levy on periodic payments of compensation needed to support the wage earner and his family on a week-to-week, month-to-month basis. There is no indication, however, that Congress intended drastically to alter the delicate balance of a debtor's protections and obligations during the bankruptcy procedure.[11] We therefore agree with the Court of Appeals that the Consumer Credit Protection Act does not restrict the right of the Trustee to treat the income tax refund as property of the bankrupt's estate. Accordingly, the judgment of the Court of Appeals is affirmed.

It is so ordered.

---

[11] Petitioner argues that, since Chapter XIII of the Bankruptcy Act had been explicitly excluded from the scope of the Consumer Credit Protection Act (see 15 U. S. C. § 1673 (b)) it must have intended to include the other portions of the Bankruptcy Act. Chapter XIII permits a wage earner to satisfy his creditors out of future income under a supervised plan. This particular procedure resembles the normal credit situation to which the CCPA is directed more than other bankruptcy situations and, for this reason, Congress might well have felt it necessary to ensure that the CCPA was not enforced at the expense of the Bankruptcy procedures.